In The

Supreme Court of The United States

October Term, 1977

No. 77-255

SUNDSTRAND CORPORATION,

Petitioner

vs.

SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., Executors of the Estate of John B. Huarisa,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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* Several of the opinions and orders entered in this litigation have been printed in the appendix to the petition for a writ of certiorari filed by Henry W. Meers (cited herein as "M. App._________"), No. 77-83, and are therefore not reprinted in this appendix. The appendix of petitioner Sundstrand Corporation, the pages of which are numbered consecutively following those of the Meers appendix (M.App. 1-109), begins at App. 110.

** Each page in the trial record cited by the Court of Appeals in Footnote 35, as amended, is included in full in this appendix, although some pages begin or end in the middle of a sentence, question, or answer.

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Petitioner Sundstrand Corporation respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit entered in this action on February 23, 1977 insofar as it pertains to defendants-respondents Sun Chemical Corporation, and Raymond F. Ryan and Thomas B. Hart, Jr., executors of the estate of John B. Huarisa.*

* Petitioner does not seek review of the judgment below insofar as it relates to defendant Henry W. Meers. Since respondents were far more deeply involved in the fraudulent conduct than was Meers during the time period upon which this petition focuses, the issues which petitioner seeks this Court to consider are more clearly presented by limiting the petition to these respondents. Meers has filed a petition for a writ of certiorari (Case No. 77-83) to which Sundstrand Corporation has responded.

OPINIONS BELOW

The opinion of the Court of Appeals is officially reported at 553 F.2d 1033 and is printed in the appendix to the petition for a writ of certiorari filed by Henry W. Meers in Case No. 77-83. (M.App 72-107)* The opinion of the United States District Court for the Northern District of Illinois, Eastern Division, from which that appeal was taken, is not officially reported and is printed at M.App. 2-71. A prior opinion of the Court of Appeals in this action, not pertinent to the issues presented by this petition, is reported *sub nom. Sundstrand Corp.* v. *Standard Kollsman Industries, Inc.* at 488 F.2d 807 (7th Cir. 1973). All references herein to the Court of Appeals' opinion are to the more recent opinion.

JURISDICTION

The judgment of the United States Court of Appeals for the Seventh Circuit sought to be reviewed was entered on February 23, 1977. (M.App. 108) A petition for rehearing and suggestion of rehearing en banc was filed by petitioner herein on March 29, 1977.** The petition for rehearing was denied on May 18, 1977.*** This petition for certiorari is filed within ninety days of that date. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

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* On April 18, 1977 and May 18, 1977 the Court of Appeals entered orders which provided for certain additions to the opinion of February 23, 1977. The opinion as officially reported reflects all such changes. The opinion as reprinted in the appendix to the petition in Case No. 77-83 (hereinafter "M.App.") does not reflect those changes. The Order of April 18, 1977 is set forth in full at M.App. 109. The Order of May 18, 1977 is set forth in full in the appendix to this petition (hereinafter "S.App.") at S.App. 110-11. Footnote 35 of the opinion of the Court of Appeals, as amended, appears at S.App. 112.

** On March 3, 1977 the Court of Appeals granted petitioner an extension of time until March 29, 1977 within which to file a petition for rehearing. That petition was directed only to the defendants who are respondents herein.

*** One member of the panel which decided the appeal voted for rehearing. One of the other Circuit Judges who considered petitioner's suggestion for rehearing en banc voted for rehearing. (S.App. 110-11)

QUESTIONS PRESENTED

1. May a plaintiff-purchaser of securities who acted in reliance on defendants' fraudulent conduct in violation of Securities and Exchange Commission Rule 10b-5, and who acted without any knowledge of that fraud, be deprived of damages resulting from that fraud because another cause may have contributed to the purchaser's consummation of the transaction which resulted in the damages?*

2. Where the defendant deliberately committed a fraud in violation of Securities and Exchange Commission Rule 10b-5, can a plaintiff-purchaser be deprived of damages resulting from that fraud on the ground that the purchaser acted negligently in consummating the purchase?

3. Can a Court of Appeals make an "independent study" of material not in the trial record in order to make findings of fact contrary to findings made by the District Court?

STATUTE AND RULE INVOLVED

Sections 10(b) and 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b) and 78cc(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5, are set forth in the appendix hereto (S.App. 113-114).

STATEMENT OF THE CASE

In August, 1969 petitioner Sundstrand Corporation ("Sundstrand") filed its complaint against Standard Kolls-

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* As presented by Question No. 3, petitioner contends that there was no evidence of any cause other than petitioner's reliance on respondents' fraud. For purposes of Question No. 1, however, the existence of another cause is assumed *arguendo*.

man Industries, Inc. ("SKI"),* John B. Huarisa ("Huarisa"),** chief executive officer of SKI, and Henry W. Meers ("Meers"), a director of SKI, alleging that all three defendants had violated Section 10(b) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder by the Securities and Exchange Commission, 17 CFR § 240.10b-5, in connection with Sundstrand's purchase of 223,190 shares of SKI stock in early 1969. The District Court's jurisdiction of the action was predicated on Section 27 of the 1934 Act, 15 U.S.C. § 78aa.

At the first trial of this action, in 1971, Sundstrand's claim was dismissed at the close of its evidence. That ruling was reversed. 488 F.2d 807 (7th Cir. 1973).

At the second trial, the District Court, sitting without a jury, found all defendants liable and entered judgment against them in the amount of $4,434,786 plus prejudgment interest. The Court of Appeals affirmed the judgment and findings of liability in all respects but reduced the amount awarded to plaintiff-petitioner to $334,785 plus prejudgment interest, a reduction of 93%. Petitioner seeks review of that Court of Appeals decision insofar as it reduced the amount of the District Court's judgment against defendants Sun and Huarisa's executors.

The fraudulent conduct of defendants which gave rise to the findings of liability by the courts below involves misrepresentations and omissions concerning the financial condition of SKI in late 1968 and early 1969. Sundstrand's involvement began in late 1968 but earlier events are pertinent to an understanding of the pervasive fraud.

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* In December, 1972, SKI was merged into respondent Sun Chemical Corporation ("Sun"). As successor to the liabilities of SKI, Sun was substituted for SKI as a defendant.

** In May, 1975, Huarisa died. His executors, respondents Raymond F. Ryan and Thomas B. Hart, Jr., were substituted for him as defendants.

1. Questions Concerning SKI's Accounting Practices

By year-end 1967, Kollsman Instrument Corporation ("KIC"), SKI's principal subsidiary, had deferred substantial preproduction costs in connection with programs for the production of certain aircraft instrumentation. In mid-1968, after publication of SKI's 1967 annual report reflecting these deferrals, James W. Burke, a director and large shareholder of SKI, and one of SKI's other directors, raised questions regarding the propriety of SKI's accounting practices and the accuracy of the financial statements. Burke formally submitted questions to the SKI board regarding those matters (the "Burke report"), as well as a report critical of SKI's accounting practices which had been prepared by the accounting firm of Ernst & Ernst (the "Ernst & Ernst report"), which Burke had retained. However, no changes were made in the accounting practices, and SKI deferred substantial additional preproduction costs throughout 1968. (Dist. Ct. at M.App. 30-32; Ct. Ap. at M.App. 83-84, 95-97)

2. SKI's Grossly False Nine-Month's Report

On November 4, 1968, SKI published its quarterly report to shareholders for the nine months ended September 30, which stated that SKI had income before taxes of $4,350,039 for the first nine months of the year with net income after taxes equivalent to $.86 per share. These figures were not audited or reviewed by Price Waterhouse & Co., SKI's independent accountants. In fact, as the District Court found, and as affirmed by the Court of Appeals, the reported nine months earnings of SKI and its subsidiaries were deliberately grossly overstated, since SKI should have reported income before taxes of only $633,756 for that period, or approximately $.12 per share after taxes. (Dist. Ct. at M.App. 34-48; Ct. Ap. at M.App. 82 n. 8)

3. Merger Negotiations Between Sundstrand and SKI and Further Misrepresentations by Defendants

In the late summer of 1968 Huarisa and SKI were searching for a company suitable for a merger with SKI. In mid-November, 1968, after publication of the third quarter report, and pursuant to Huarisa's authorization, Meers, an SKI director, contacted Sundstrand to see if it was interested in a merger with SKI. Thereafter, a number of meetings were held in November and December, 1968 among representatives of Sundstrand and Huarisa and other SKI representatives. During these meetings Huarisa represented to Sundstrand that SKI's earnings for the first three quarters of 1968 were $.86 per share, as reported in the published nine months' earnings statement. Huarisa also told Sundstrand that SKI's net income for all of 1968 would be between $2,600,000 and $2,900,000, that SKI's 1968 earnings per share would be about $1.16, and that SKI's earnings for the year 1969 would be about $2.41 or even $2.50 per share. Huarisa provided a written projection to Sundstrand which showed 1969 earnings of $2.13 per share. Huarisa also stated that in no case would there be adjustment to 1968 earnings which would reduce them below the $.86 per share already reported. As both the District Court and the Court of Appeals held, Huarisa and SKI knew or were reckless in not knowing that the 1968 and 1969 earnings projections were grossly inflated. (Dist. Ct. at M.App. 7-11, 28-30, 60; Ct. Ap. at M.App. 76-77, 82)

Thereafter, Sundstrand representatives commenced merger negotiations with Huarisa and Meers which culminated in an offer by Sundstrand for the assets of SKI subject to its liabilities for Sundstrand stock equivalent to $38.25 per SKI share. This proposal was subject to, *inter alia,* Sundstrand's conducting a survey of the business of SKI. On January 2, 1969, the SKI board authorized Hua-

risa to proceed on the basis of the Sundstrand proposal. (Dist. Ct. at M.App. 10-13; Ct. Ap. at M.App. 77)

4. Huarisa's Right of First Refusal

Huarisa owned a block of SKI stock and a right of first refusal on additional shares of SKI common stock owned by the Burke family interests. On December 10, 1968 Huarisa had received from the Burke family an offer to sell to him, at $30 per share, 223,190 shares of SKI stock covered by Huarisa's right of first refusal. Under that right Huarisa had 30 days within which to exercise his right by paying 5% of the purchase price. Otherwise, Sun, which had made the offer to the Burkes, would have an unconditional right to purchase the stock. (Dist. Ct. at M.App. 5, 13-14; Ct. Ap. at M.App. 75)

On January 4, 1969, Huarisa first informed Sundstrand that there was a right of first refusal which had been triggered by an offer by a third party. At a meeting on January 6, 1969 Huarisa advised Sundstrand that if Sun acquired the stock from the Burkes, Sundstrand and SKI would have to forget about the proposed merger. As both courts below held, after receiving Huarisa's confirmation that SKI's 1968 and 1969 earnings projections still looked good, Sundstrand orally agreed to acquire Huarisa's right of first refusal on 223,190 shares of SKI stock at $30 per share. (Dist. Ct. at M.App. 13-15, 18; Ct. Ap. at M.App. 75, 85-87, 102)

Accordingly, on January 8, 1969 Huarisa exercised his right of first refusal by delivering to the Burke family his written election to purchase and $334,785 in cash, representing 5% of the purchase price. On January 9, 1969 Sundstrand and Huarisa entered into a written agreement reflecting the oral agreement of January 4, 1969. (Dist. Ct. at M.App. 15-16; Ct. Ap. at M.App. 75-76)

5. Sundstrand's Survey of SKI and Still Further Misrepresentations and Omissions

Sundstrand undertook a survey of SKI to determine whether or not the merger should be consummated. As both the District Court and the Court of Appeals held, the financial information regarding KIC and SKI which was provided to Sundstrand during the survey and on which Sundstrand relied was deliberately restricted and was misleading, and Huarisa and the principal financial officers of SKI and KIC, including Raymond Ryan, conspired to prevent Sundstrand from discovering SKI's true financial condition. Indeed, Sundstrand's questions about SKI's financial condition were often answered with outright lies. (Dist. Ct. at M.App. 19-22, 48-57; Ct. Ap. at M.App. 77, 79, 82, 84 n. 10)

6. Termination of Merger Negotiations and Stock Purchase

After Sundstrand personnel evaluated the information provided by SKI, they concluded on January 20, 1969 that certain aspects of the proposed transaction, including an increase in labor costs which a merger would cause, undesirable SKI labor practices and lack of the expected compatibility of SKI's and Sundstrand's products, and a belief on the part of Sundstrand that SKI's earnings projections were somewhat optimistic, made the acquisition unattractive. A decision was then made to cancel the negotiations. (Dist. Ct. at M.App. 22-23; Ct. Ap. at M.App. 77)

Despite further misrepresentations and omissions regarding SKI's financial condition by Huarisa and Ryan at meetings on January 20 and 22, 1969, Sundstrand adhered to its decision to call off the merger negotiations. However, at the close of the January 22 meeting Sundstrand's president indicated that Sundstrand was going to purchase the shares covered by the right of first refusal. On February 6, 1969 Sundstrand made its payment of $6,360,915 for the

223,190 shares of SKI common stock. Both Huarisa and Ryan were aware of and participated in the consummation of that transaction. (Dist. Ct. at M.App. 23-25, 48 *et seq.;* Ct. Ap. at M.App. 78-79, 82-85)

7. SKI's Massive 1968 Loss and Sundstrand's Discovery of the Misrepresentations and Omissions

On March 21, 1969 SKI published its 1968 annual report which reported an after tax *loss* of $798,803, equivalent to a loss of $.15 per share after taxes (M.App. 25), as contrasted with Huarisa's earlier projection of a profit of $1.16 per share. The disparity between the previously reported earnings and the loss was caused by substantial write-offs taken as of year-end 1968.

After the foregoing events, and only in pre-trial discovery herein, Sundstrand learned that during January and early February 1969, Price Waterhouse was advising SKI, Huarisa and other officers of SKI that substantial year-end write-offs would have to be made on the books of SKI, which would adversely affect SKI's earnings for 1968 by several million dollars. Several days prior to Sundstrand's cash payment of $6,360,915 for the SKI stock on February 6, 1969, Ryan, principal financial officer of SKI, and his counterpart at KIC received a memorandum from Price Waterhouse stating its preliminary assessment that write-offs in the range of $3 million to $4.5 million would have to be made on the books of SKI as of year-end 1968 and stating that it was encountering new areas of concern almost daily. As the District Court found and the Court of Appeals affirmed, Huarisa also knew of this assessment before February 6, 1969. (Dist. Ct. at M.App. 48-51; Ct. Ap. at M.App. 84-85) Yet, no one—neither Huarisa nor Ryan nor anyone else—disclosed the Price Waterhouse assessment to Sundstrand. The Court of Appeals held that "[t]he memorandum should have been disclosed to Sund-

strand." (M.App. 84) In large part the write-offs accounting for the difference between the fraudulent profit projection made to Sundstrand and the actual loss had been outlined in the undisclosed Price Waterhouse memorandum. In addition, only in March, 1969, after the loss for 1968 was reported, did Sundstrand learn of James Burke's criticisms of SKI's accounting practices and of the Burke and Ernst & Ernst reports. Those reports had criticized the deferral of certain preproduction costs which were part of the substantial write-offs as of year-end 1968. (Dist. Ct. at M.App. 25-26; Ct. Ap. at M.App. 83-84, 95-97)

8. The District Court's Findings and Judgment

After a lengthy trial the District Court held in an extensive opinion that all of the defendants had violated Rule 10b-5 in misrepresenting material facts to Sundstrand and failing to disclose material facts to Sundstrand through the date of Sundstrand's purchase of the SKI stock on February 6, 1969. (M.App. 60 *et seq.*) The District Court found that SKI and Huarisa intentionally overstated earnings as of September 30, 1968, recklessly projected earnings for 1968 and 1969 and deliberately withheld the Price Waterhouse memorandum and the Burke and Ernst & Ernst reports. The District Court also held that Sundstrand had no knowledge of these misrepresentations and omissions prior to the purchase. (M.App. 57)

The District Court thus concluded that Sundstrand had been wrongfully induced to purchase the SKI stock. It ruled that the damages were the difference between the amount paid for the SKI stock and its actual value. The District Court awarded damages of $4,434,786, plus prejudgment interest at the rate of 6% per annum from February 6, 1969. (M.App. 70-71) (As of the date of this petition that judgment would aggregate over $6,700,000.)

9. The Court of Appeals' Opinion and Judgment

All defendants appealed from the judgment of the District Court. The Court of Appeals affirmed the judgment of liability as to all defendants in all respects. However, the Court of Appeals held that Sundstrand was only entitled to recover damages with respect to the initial payment for the stock made by Sundstrand as a result of its January 9, 1969 agreement with Huarisa, namely $334,785, plus prejudgment interest at 6% per annum from January 9, 1969. (M.App. 106-108) (On July 21, 1977, the amount of that judgment was paid by Sun. By this petition Sundstrand seeks to recover the balance of the judgment awarded by the District Court.)

The sole rationale for the reduction in damages by over 90% was the Court of Appeals' *sua sponte* finding that the "only" or "principal" reason why Sundstrand completed the purchase of the stock on February 6, 1969 was that Sundstrand had relied on an erroneous opinion of counsel to the effect that under the January 9, 1969 agreement between Sundstrand and Huarisa, Sundstrand was obligated to complete the purchase.* The District Court had made no findings as to any such opinion, and the parties had not briefed such an issue on appeal. (M.App. 103-104) This ruling by the Court of Appeals that there was a "superseding cause"—based upon its "independent study of the record"—was contrary to the express findings by the District Court that Sundstrand continued to rely upon the misrepresentations and omissions made by the defendants when Sundstrand made its final payment for the stock in question, on February 6, 1969, that such reliance was entirely reasonable, and that Sundstrand did not begin to learn the truth regarding defendants' fraud or the horrendous financial condition of SKI until late March, 1969. (M.App. 56-58)

* Both the District Court and the Court of Appeals had concluded that Sundstrand was not obligated to make any further payments under the agreement with Huarisa after reimbursing him for the downpayment he had made. (Dist. Ct. at M.App. 18, 25; Ct. Ap. at M.App. 102)

REASONS FOR GRANTING THE WRIT

Each of the three reasons for granting the requested writ of certiorari involves not only an erroneous ruling below but a direct conflict between the decision below and the decisions of other Courts of Appeals on significant matters involving the federal securities laws and the scope of appellate review. The decision below also conflicts with decisions of this Court. Review by this Court is necessary to resolve these conflicts and to correct the errors below.

I. The Causation Analysis Upon Which The Seventh Circuit's Decision Rests Is In Conflict With This Court's Decisions Under The Federal Securities Laws And With Decisions In Other Circuits, And Is Demonstrably Erroneous

The ruling below ignored the principles of causation applicable to actions under Rule 10b-5 enunciated by this Court and by other Courts of Appeals in holding that the presence of an additional cause, i.e. a cause in addition to plaintiff's reliance on defendants' misconduct, precludes recovery in an action under Rule 10b-5 even where the plaintiff-purchaser had no knowledge of the deliberate misrepresentations and omissions perpetrated by the defendants. Review of the decision below is necessary to clarify the applicable principles of causation and to correct this error, just as this Court has recently resolved the three other principal legal issues in private actions under Rule 10b-5.* This case presents a particularly favorable setting for a definitive resolution of causation standards in such cases. No issue of fact is presented by Question No. 1, since,

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* The principal legal questions which have arisen in cases under Rule 10b-5 are plaintiff's standing, the culpability required on the part of the defendant, the definition of a "material" fact and the relevance of traditional tort concepts of causation, including reliance. This Court has recently specifically addressed itself to the first three of these issues. *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 183 (1976); and *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438 (1976) (under SEC Rule 14a-9, 17 C.F.R. § 240.14a-9).

for purposes of this issue, petitioner accepts *arguendo* the Court of Appeals' erroneous and unsupported finding that petitioner had relied on an opinion of counsel in consummating the transaction. (*See* pp. 21-23, *infra*)

Although there was some analysis of causation in actions under Rule 10b-5 in *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972), much confusion remains surrounding the application of traditional tort principles of causation in such actions. For example, *compare Shapiro* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 495 F.2d 228, 238-242 (2d Cir. 1974), with *Fridrich* v. *Bradford,* 542 F.2d 307, 316-320 (6th Cir. 1976), *cert. denied,* 97 S.Ct. 767 (1977). *See generally* 1 A. Bromberg, *Securities Law: Fraud,* Secs. 4.7(550) *et seq.* (1973); 5 Jacobs, *The Impact of Rule 10b-5,* § 64.02 (1976). *See also* cases cited at pp. 17-18, *infra.* While some of the cited cases involve causation issues in contexts other than that presented by the instant case, the need for this Court to clarify causation standards in actions under Rule 10b-5 is apparent. Moreover, since this case involves a single plaintiff defrauded in a face-to-face transaction (as distinguished from, e.g., a class action or an open market transaction), it presents more fundamental issues than do many other cases in which causation questions arise, and therefore is particularly suitable for consideration by this Court.

A. The Decision Below Is In Conflict With This Court's Decision In *Affiliated Ute Citizens v. United States,* 406 U.S. 128 (1972), And With Decisions Of Other Circuits

The correct application of this Court's analysis of causation in *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972), to the facts of this case can be demonstrated by a single but crucial example of an actionable non-disclosure. Both the Court of Appeals and the District Court held that SKI and Huarisa intentionally withheld from Sundstrand

the January 27, 1969 Price Waterhouse memorandum, an obviously material document which indicated huge anticipated write-offs at year-end 1968 about which Sundstrand had no knowledge. Both courts also held that Huarisa and Ryan knew of the memorandum and knew that Sundstrand was about to pay the balance of the purchase price for the SKI stock which was subject to the right of first refusal. (Dist. Ct. at M.App. 24, 49-50; Ct. Ap. at M.App. 78, 84) "This obligation to disclose and this withholding of a material fact established the requisite element of tort causation in fact." *Affiliated Ute Citizens, supra,* 406 U.S. at 154 (1972).* *See also Piper* v. *Chris-Craft Industries, Inc.,* 97 S.Ct. 926, 953-54 (1977) (Blackmun, J., concurring in the judgment).

Many lower federal courts have held that reliance upon the misrepresentation or omission at issue need not be the *sole* cause of plaintiff's damage in order to sustain a cause of action under Rule 10b-5; it need only be a substantial factor. *Herzfeld* v. *Laventhol, Krekstein, Horwath & Horwath,* 540 F.2d 27, 34 (2d Cir. 1976); *Mitchell* v. *Texas Gulf Sulphur Co.,* 446 F.2d 90, 102 (10th Cir. 1971), *cert. denied,* 404 U.S. 1004 (1972); *McLean* v. *Alexander,* 420 F.Supp. 1057, 1077 (D.Del. 1976); *see also Zenith Radio Corp.* v. *Hazeltine Research, Inc.,* 395 U.S. 100, 114 n. 9 (1969) ("It is enough that the illegality is shown to be *a* material cause of the injury. . . ."; emphasis added).

Under the *Affiliated Ute Citizens* presumption and the cases cited in the preceding paragraph, the conduct referred to above, as well as respondents' other acts in violation of Rule 10b-5, constitutes at least *a* cause of Sundstrand's

* While proof that plaintiff had actual knowledge of the omitted facts (*Sanders* v. *John Nuveen & Co., Inc.,* 524 F.2d 1064, 1073 (7th Cir. 1975), *vacated and remanded on other grounds,* 425 U.S. 929 (1976)) or that plaintiff would have made the purchase even if he had known the undisclosed facts (*Rochez Bros., Inc.* v. *Rhoads,* 491 F.2d 402, 410-11 (3d Cir. 1974)) might rebut the *Affiliated Ute Citizens* presumption of causation, neither circumstance was present here. (M.App. 57) *See also pp. 17-20, infra.*

purchase of the SKI stock and *a* cause of the resulting loss. No more need be proven. Under the cases cited in the preceding paragraph, even if some other cause (e.g. reliance on a legal opinion regarding Sundstrand's obligation to make the purchase) was operating at the same time, because respondents' conduct was an operating cause, Sundstrand was entitled to recover from respondents. Accordingly, the decision below (1) erred in failing to follow *Affiliated Ute Citizens* and (2) was inconsistent with the decisions cited in the preceding paragraph. Review by this Court is necessary to resolve the conflict and to clarify the holding of *Affiliated Ute Citizens.*

B. Correct Application Of This Court's Holding In *Mills v. Electric Auto-Lite Co.,* 396 U.S. 375 (1970), Demonstrates That There Was No Exculpatory "Superseding" Cause

The Court of Appeals also failed to perceive that its finding of an exculpatory, second cause was in conflict with still another decision of this Court, *Mills* v. *Electric Auto-Lite Co.,* 396 U.S. 375 (1970).

The Court of Appeals *sua sponte* raised the question whether any reliance by Sundstrand on an opinion of counsel to the effect that Sundstrand was contractually obligated to complete the purchase constituted a "superseding cause" which exonerates Sun and Huarisa.* (M.App. 105) The concept of "superseding cause," which in certain limited circumstances will relieve a prior wrongdoer of liability for injury to which his misconduct has made a substantial contribution, was developed in negligence cases at common law. Even in such cases, in order to "supersede" the initial wrongdoer's liability, the later cause must be

* As shown at pp. 21-23, *infra,* not only was the Court of Appeals' finding unsupported by the evidence, but the evidence established that *there was no such opinion.*

one *not* produced or set in motion by the initial wrongful act, but rather must be of independent origin. *Restatement (Second) of Torts*, §§ 440-42 (1965); Prosser, *Law of Torts*, § 44, at 270-71 (4th ed. 1971); *Freeman* v. *United States*, 509 F.2d 626, 633-34 (6th Cir. 1975); 22 Am.Jur.2d, "Damages," § 84 at 120 and § 111 at 161-62 (1965); *Comstock* v. *General Motors Corp.*, 99 N.W.2d 627, 635-36 (Mich.Sup.Ct. 1959).

In the present case, any reliance on counsel was not a "superseding cause" even as that concept has been applied in negligence cases. Regardless of any understanding that Sundstrand may have had concerning the interpretation of the January 9, 1969 agreement with Huarisa, if Sundstrand or its counsel had been informed, before February 6, 1969, of the gross deception in violation of Section 10(b) which had been practiced on Sundstrand by the conspiratorial actions of SKI and Huarisa and which (as both courts held) had induced Sundstrand to enter into the agreement in the first instance, Sundstrand and its counsel would also have known that the agreement with Huarisa was voidable under Section 29(b) of the 1934 Act, 15 U.S.C. § 78cc(b) (S.App. 113), as interpreted by this Court in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 382-88 (1970), following *Bankers Life & Cas. Co.* v. *Bellanca Corp.*, 288 F.2d 784, 787 (7th Cir. 1961). Thus, the supposed "superseding" cause of counsel's opinion found by the Court of Appeals would have disappeared altogether had Huarisa or SKI disclosed (or had Sundstrand otherwise learned of) the wrongful conduct found by both courts below. The Court of Appeals' ruling in effect allows respondents to escape liability by reason of a "cause" created by and kept in effect solely by their own continuing misconduct. Therefore, the Court of Appeals erred in holding that there was an exculpatory second, or superseding, cause.

At most, then, any reliance on counsel was a concurrent cause with Sundstrand's reliance on defendants' misrepre-

sentations and omissions. Where harm results from two concurrent, equally sufficient causes, even a negligent wrongdoer is liable regardless of any negligence on the part of the second actor. *Restatement (Second) of Torts,* § 432(2) (followed in *Basko* v. *Sterling Drug, Inc.,* 416 F.2d 417, 429-30 (2nd Cir. 1969)) and §§ 302A, 439 and 442 (1965); 2 Harper & James, *The Law of Torts,* § 20.2 at 1123 (1956); Prosser, *Law of Torts,* § 44 at 274 (4th ed. 1971). Since such a rule embraces merely negligent wrongdoers, *a fortiori* an intentional or reckless wrongdoer should not escape liability under such circumstances.

This Court should grant a writ of certiorari here in order to reaffirm *Mills* and to clarify the role (if any) of the concepts of "concurrent" and "superseding" causes in actions under Rule 10b-5.

II. The Decision Below Is In Conflict With Decisions Of Other Circuits Interpreting This Court's Decision In *Ernst & Ernst v. Hochfelder,* 425 U.S. 183 (1976), As It Relates To Plaintiff's Conduct As A Defense

The decision below is also in conflict with another line of recent appellate decisions under Rule 10b-5. Prior to this Court's decision in *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 183 (1976), a number of courts had held that a plaintiff's mere lack of diligence in discovering the truth was a defense in an action under Rule 10b-5. E.g., *Clement A. Evans & Co.* v. *McAlpine,* 434 F.2d 100, 103 (5th Cir. 1970), *cert. denied,* 402 U.S. 988 (1971); *see generally* Wheeler, "Plaintiff's Duty of Due Care Under Rule 10b-5: An Implied Defense to an Implied Remedy," 70 *Nw.U.L.Rev.* 561 (1975). As a result of *Hochfelder,* which requires proof of scienter on the part of the defendant, however, several Courts of Appeals have reconsidered the due diligence defense.

In *Holdsworth* v. *Strong,* 545 F.2d 687 (10th Cir. 1976) (en banc), *cert. denied,* 97 S.Ct. 1600 (1977), the Court of Appeals held, "[i]f contributory fault of plaintiff is to can-

cel out wanton or intentional fraud, it ought to be gross conduct somewhat comparable to that of defendants." 545 F.2d at 693. Similarly, in *Dupuy* v. *Dupuy,* 551 F.2d 1005, 1020 (5th Cir. 1977), the court held that a Rule 10b-5 plaintiff will be barred only if his conduct is reckless; the issue is whether the plaintiff "intentionally refused to investigate 'in disregard of a risk known to him or so obvious that he must be taken to have been aware of it, and so great as to make it highly probable that harm would follow,'" not merely whether plaintiff acted unreasonably. 551 F.2d at 1020. *Contra, Hirsch* v. *duPont,* 553 F.2d 750, 763 (2d Cir. 1977) (plaintiff barred for "fail[ure] to exercise due diligence"), followed in *NBI Mortgage Investment Corp.* v. *Chemical Bank,* CCH Fed. Sec. L.Rep. ¶ 96,066, at p. 91,801 (S.D.N.Y. 1977) [Current Binder] (refused to follow *Holdsworth,* holding that under *Hirsch* "the standard of due diligence is still viable and accepted in this circuit"); *see Straub* v. *Vaisman & Co., Inc.,* 540 F.2d 591, 596-98 (3d Cir. 1976) (the issue is whether plaintiff "acted reasonably"); and *McLean* v. *Alexander,* 420 F.Supp. 1057, 1078 (D.Del. 1976) (plaintiff is "charged with a duty of due diligence commensurate with his investor sophistication"), all after *Hochfelder.*

The opinions cited above demonstrate that, depending on the court in which he sues, a plaintiff may be barred from recovery merely for failing to exercise diligence, or for acting unreasonably or only for acting recklessly. This aspect of the implications of *Hochfelder* is clearly ripe for, and merits, review by this Court.

In the instant case, the Court of Appeals purported to adopt the *Holdsworth* test (M.App. 100), but neither the result nor the court's reasoning accorded with that standard. There is no basis for a conclusion that Sundstrand acted recklessly or with gross conduct, and neither court below so found. While the Court of Appeals suggested that Sundstrand had some information contrary to defendants' repre-

sentations (M.App. 82-83, 104), in fact, as the District Court found, "[t]here is no evidence whatsoever that Sundstrand had actual knowledge of the fraud being perpetrated upon it," and its reliance on defendants' statements was "entirely reasonable." (M.App. 57, 58) Sundstrand's difference of opinion with SKI on the exact magnitude of SKI's likely earnings for 1968* does not constitute any bar to Sundstrand's recovery under the standard enunciated in *Holdsworth* and *Dupuy*. Any reliance on an erroneous legal opinion would also not have been gross or reckless conduct.

Contrary to the evidence, the Court of Appeals found that Sundstrand "had learned enough to apprise it that forfeiture of its down payment was better than further payments" under the agreement with Huarisa. (M.App. 104) The evidence is clear that Sundstrand in fact concluded, after the termination of merger negotiations and before the February 6 payment, that purchase of the SKI shares was "a good investment." (Schuette Dep. 330-33, 336-37, Miller at Trial Tr. 749-52, S.App. 155-159, all of which was in evidence) In addition, as the District Court found, Huarisa had advised Sundstrand, albeit falsely, that other companies had offered $45 per share for SKI, and the $30 per share price was far below Sundstrand's own $38.25 merger proposal. (M.App. 10) At most, the contrary conclusion of the Court of Appeals reflects a difference of opinion on a matter of business judgment, which is a patently inadequate basis under *Holdsworth* and *Dupuy* for overturning the District Court's damage award.

By thus purporting to adopt a high standard of proof to establish the defense (*Holdsworth*) but in fact applying

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* While Sundstrand lacked confidence in Huarisa's statement that SKI's 1968 earnings would be $1.16 per share, Sundstrand merely concluded that SKI was more likely to earn $.80 to $1.00 a share and, because that conclusion was based on the numerous false statements and omissions of SKI and Huarisa which Sundstrand believed to be true, it had no inkling that SKI would *lose* $.15 per share. (M.App. 23)

a low standard of proof, the Court of Appeals watered down the "gross conduct" test so as to evade an obvious implication of the holding in *Hochfelder*—an erosion no less pernicious for its indirectness.* This Court should resolve the conflict involving five Courts of Appeals and determine the parameters of any defense in Rule 10b-5 actions based on plaintiff's conduct.**

III. The Court Of Appeals' Reversal Of The District Court Based Upon The Court Of Appeals' Independent Examination of Material Not In The Trial Record Conflicts With Decisions Of Other Circuits And Warrants Exercise Of This Court's Supervisory Power.

The Court of Appeals' ruling that Sundstrand was not entitled to recover damages for the February 6, 1969 payment was based on that court's finding that Sundstrand consummated the purchase "only" because it believed, based on an opinion of counsel, that it was legally obligated to do so. (M.App. 103) This finding, developed from that court's "independent study of the record" (M.App. 103), was in the face of the District Court's contrary findings on reliance and causation.*** *This crucial finding of reliance on an opinion of counsel, a finding the defendants did not*

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* The approach by this panel of the Court of Appeals should be contrasted with the admonition of another panel of the same court:

> [T]he definition of "reckless behavior" should not be a liberal one lest any discernible distinction between "scienter" and "negligence" be obliterated for these purposes. We believe "reckless" in these circumstances comes closer to being a lesser form of intent than merely a greater degree of ordinary negligence. We perceive it to be not just a difference in degree, but also in kind. *Sanders* v. *John Nuveen & Co., Inc.*, 554 F.2d 790, 793 (7th Cir. 1977) (on remand from Supreme Court).

** Meers, petitioner in the related case, No. 77-83, presents a similar question in his Question No. 2.

*** *See, e.g.*, M.App. 56-58. In this ruling, the Court of Appeals also failed to adhere to the requirements of Rule 52(a), F.R.Civ.P., that "findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses."

seek and no party briefed on appeal, was expressly, indeed blatantly, predicated upon material not in the trial record **and thus not within the Court of Appeals' scope of review.**

The Court of Appeals' express ruling that it can independently consult evidentiary material not in the trial record and make its own findings of fact based thereon (S.App. 111) is in square conflict with decisions of other Courts of Appeals. (*See* pp. 22-23, *infra*) Moreover, such conduct constitutes, in the words of Supreme Court Rule 19, a "depart[ure] from the accepted and usual course of judicial proceedings . . . [so far] as to call for an exercise of this Court's power of supervision."

> **This Court is charged with supervisory functions in relation to proceedings in the federal courts. See McNabb v. United States, 318 U.S. 332, 63 S.Ct. 608, 87 L.Ed. 819. Therefore, fastidious regard for the honor of the administration of justice requires the Court to make certain that the doing of justice be made so manifest that only irrational or perverse claims of its disregard can be asserted. (*Communist Party* v. *Subversive Activities Control Board,* 351 U.S. 115, 124 (1956).)**

This Court should exercise its supervisory powers in order to prevent the conduct by the Court of Appeals herein from becoming a pernicious precedent for appellate review of findings of fact.

The court below cited numerous references to the record on appeal* to support the result of its "independent study of the record." (M.App. 104 n. 35 and S.App. 112) But of the twenty-five citations therein to transcript or deposition pages, only five were to trial testimony or to depositions *in evidence*. (The texts of the twelve passages of the twenty-five which are in the trial record are set forth in the

*** Pursuant to Rule 10(a), F.R.App.P., the record on appeal included all papers filed in the District Court since this case was commenced in 1969. *International Business Machines Corp.* v. *Edelstein*, 526 F.2d 37, 45 (2d Cir. 1975).**

appendix to this petition at S.App. 116-147) The Court of Appeals' only citations to evidence in the trial record were Trial Tr. 131, 165-67, 484-87 and 625-31 and Huarisa Dep. 229-30. (S.App. 116-128, 146-147) Only two of these five passages in evidence so much as refer to an opinion of counsel. Neither of the two supports the Court of Appeals' finding that the "only" or "principal reason" Sundstrand completed the purchase was "because counsel had wrongly advised Sundstrand officials that it was legally obligated" to make the purchase.* (M.App. 103) There is no other *evidence* in the *trial record* bearing on any opinion of counsel. The remaining citations to the trial transcript in original footnote 35 of the Court of Appeals opinion are to argument of counsel or to colloquy. (S.App. 128-146) The other thirteen citations are to deposition passages not admitted or even offered into evidence at trial.

Other Courts of Appeals have consistently held that they cannot consider evidentiary material not in the actual trial record in appraising the District Court's findings, much less to formulate their own findings of fact. *United States* v. *City of Brookhaven,* 134 F.2d 442, 446-47 (5th Cir. 1943) (depositions not in evidence could not be considered by reviewing court even though they were included in the record on appeal); *Worsham* v. *Duke,* 220 F.2d 506, 509 (6th

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* During cross-examination of Sadler, a Sundstrand officer, counsel for Sun and Huarisa read a passage of Sadler's deposition to refresh his recollection. Sadler had testified at the deposition that Ethington, another Sundstrand officer, told Sadler that counsel felt Sundstrand was obligated to buy the stock. Sadler's recollection was not refreshed. (Tr. 484-87, S.App. 119-122) During cross-examination of Ross, counsel for Sun and Huarisa sought indirectly to *impeach* Ethington by having Ross, a Sundstrand officer, identify Sundstrand's interrogatory answer (Sun-Huarisa Ex. 52, set forth in full in the appendix to this petition at S.App. 148-151), in which Sundstrand ***DENIED that it had received an opinion of counsel in this regard***. (Tr. 625-31, S.App. 122-128) These two references provide no basis for rejecting the District Court's findings of reliance and causation. Indeed, such evidence established that there was no reliance on any such opinion because ***there was no opinion***.

Cir. 1955). *See also Rommel-McFerran Co. Inc.* v. *Local U. No. 369 Int. Bro. of Elec. Wkrs.*, 361 F.2d 658, 661-62 (6th Cir. 1966). On a previous occasion even the Court of Appeals which decided the instant case recognized this fundamental principle of appellate review. *Charles* v. *Judge & Dolph, Ltd.*, 263 F.2d 864, 867 (7th Cir. 1959).

This Court has recently criticized Courts of Appeals for relying on material not developed in the record before an administrative agency when reviewing a determination by the agency. *E. I. du Pont de Nemours & Company* v. *Collins*, 97 S.Ct. 2229, 2235 (1977) (court erred in retaining professor after oral argument to prepare reports which "had not been examined and tested by the traditional methods of the adversary process"); *F.P.C.* v. *Transcontinental Gas Pipe Line Corp.*, 423 U.S. 326, 331-32 (1976).

The unfairness of the approach by the Court of Appeals here is manifest, since Sundstrand never needed, and therefore made no effort, to rebut or to explain the material not in evidence. In any event, the evidence in the trial record, introduced by defendants, established that no legal opinion was sought or received by Sundstrand, and none was relied on.

When the Court of Appeals denied Sundstrand's petition for rehearing en banc on May 18, 1977 by a divided vote both of the members of the panel which decided the case and of other Circuit Judges, the court expanded its footnote 35 by citing cases which purportedly justify such an excursion beyond the trial record and by citing two instances where Sundstrand referred in briefs to material not in evidence.* (S.App. 111-112) The court's effort to justify its impermissible approach lacks any persuasive force.

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* The two cited instances when Sundstrand referred to filings not in evidence were references to an interrogatory answer and to a brief in the trial court. (These excerpts are set forth in the appendix to this petition at S.App. 152-154) These were cited to show contentions made in the District Court. In neither instance did Sundstrand even purport to rely on those portions of the record on appeal as evidence to prove an evidentiary fact in issue.

The opinion in *Lyon* v. *Carey*, 533 F.2d 649, 652 (D.C. Cir. 1976), does not indicate what use the District Court made of the deposition which was referred to by the Court of Appeals, but it appears that the portion of the deposition on which the Court of Appeals relied pertained to facts not in dispute on appeal. In *Merola* v. *Atlantic Richfield Company*, 515 F.2d 165, 170-71 (3d Cir. 1975), the Court of Appeals made reference to depositions in order to provide the District Court with some guidance in connection with proceedings upon remand. (In the instant case the Court of Appeals made a final determination on a factual issue without ordering a remand.) Moreover, in that case (unlike this case) it was not clear what had been and had not been included in the trial record. Finally, in *Barrett* v. *Baylor*, 457 F.2d 119, 124 n. 2 (7th Cir. 1972), the Court of Appeals considered pleadings—not depositions—in an action in a related state case which, the court noted, were properly the subject of judicial notice in any event. In short, nothing in the expanded footnote 35 excuses the Court of Appeals' egregious departure from the confines of the trial record.

This Court should grant this petition in the exercise of its supervisory powers over lower federal courts and reverse the judgment below.

CONCLUSION

For the reasons given, petitioner Sundstrand Corporation prays that a writ of certiorari be granted to review the judgment and opinion below.

Respectfully submitted,

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APPENDIX

I. OPINIONS

United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

May 18, 1977.

Before

Hon. THOMAS E. FAIRCHILD, Chief Judge
Hon. LUTHER M. SWYGERT, Circuit Judge
Hon. WALTER J. CUMMINGS, Circuit Judge

SUNDSTRAND CORPORATION, *Plaintiff-Appellee,* Nos. 76-1317, 76-1318 vs. SUN CHEMICAL CORPORATION, RAYMOND F. RYAN, THOMAS B. HART, JR., *Defendants-Appellants.*	**Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.** **No. 69 C 1660** **Bernard M. Decker, Judge.**

ORDER

On consideration of the petition for rehearing and suggestion for rehearing *en banc* filed in the above-entitled cause by appellee Sundstrand Corporation, and on consideration of the answer thereto filed by appellants Sun Chemical Corporation and Huarisa Estate, a majority of the judges of the original panel have voted to deny a rehear-

ing, and a majority of the judges in active service have voted to deny a rehearing *en banc*. Accordingly,

IT IS ORDERED that the aforesaid petition for rehearing be, and the same is hereby, DENIED.*

IT IS FURTHER ORDERED that the following be added at the end of the last line of footnote 35 of the slip opinion:

> "Some of these references are to the original transcripts of depositions that were included in the record on appeal without objection. Sundstrand has referred to such materials (Br. 77 and Pet. 10), and other courts of appeals have also referred to deposition transcripts which were in the record on appeal but not in the trial record. *E.g., Lyon* v. *Carey,* 533 F.2d 649, 652 (D.C. Cir. 1976); *Merola* v. *Atlantic Richfield Co.,* 515 F.2d 165, 170 (3d Cir. 1975); see also *Barrett* v. *Baylor,* 457 F.2d 119, 124 n. 2 (7th Cir. 1972)."

Chief Judge Fairchild voted for rehearing by the panel, Judge Bauer voted for rehearing *en banc,* and Judge Tone disqualified himself from consideration of the petition.

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* See *Santa Fe Industries, Inc.* v. *Green,* ______ U.S. ______, ______, 45 LW 4317, 4321; *Piper* v. *Chris-Craft Industries, Inc.,* ______ U.S. ______, ______, 45 LW 4182, 4195 (Blackmun J., concurring).

Footnote 35 of Court of Appeals Opinion, as Amended by Order of May 18, 1977

[The following sentence appears in the opinion of the Court of Appeals at Meers App. 103-104: "Our independent study of the record shows that the principal reason Sundstrand proceeded to purchase the Burke stock on February 6 was because counsel had wrongly advised Sundstrand officials that it was legally obligated to do so under the January 9 agreement with Huarisa.[35]" The original text of footnote 35 was expanded by the May 18, 1977 Order of the Court of Appeals and reads in its entirety as follows:]

See Tr. 131, 165-167, 484-487, 625-631, 1703-1705, 2022-2023, 2420-2423, 2516-2519, 2620-2622, 2624-2627, 2635-2638 and the following depositions: Ethington 559, 565-571, 573-574, Olson 34-38, 40, 68-69, Huarisa 229-230, Pitte 96-97, 116-117, 167-168, 171-173, 180-181 and Schuette 304-305, 306-313. As we learned at oral argument, no formal written opinion was submitted by Sundstrand's counsel as to whether Sundstrand was or was not obligated to make further payments on February 6 (Sun-Huarisa Exhibit 52). Some of these references are to the original transcripts of depositions that were included in the record on appeal without objection. Sundstrand has referred to such materials (Br. 77 and Pet. 10), and other courts of appeals have also referred to deposition transcripts which were in the record on appeal but not in the trial record. *E.g., Lyon* v. *Carey,* 533 F.2d 649, 652 (D.C. Cir. 1976); *Merola* v. *Atlantic Richfield Co.,* 515 F.2d 165, 170 (3d Cir. 1975); see also *Barrett* v. *Baylor,* 457 F.2d 119, 124 n. 2 (7th Cir. 1972).

II. STATUTE AND RULE

Section 10(b) of the Securities Exchange Act of 1934 15 U.S. § 78j(b)

It shall be unlawful for any person, directly or indirectly, by the use of any means of instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(b)

(b) Every contract made in violation of any provision of this title or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule or regulation; Provided, (A) that no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed

pursuant to paragraph (2) or (3) of subsection (c) of section 15 of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 15 of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within 3 years after such violation.

Rule 10b-5
17 C.F.R. § 240.10b-5

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

III. TEXT OF MATERIAL IN THE TRIAL RECORD CITED IN FOOTNOTE 35 OF COURT OF APPEALS OPINION, AS AMENDED BY ORDER OF MAY 18, 1977

A. Glossary of Persons Referred to in the Record Citations Listed in Footnote 35 of the Court of Appeals Opinion or Contained in this Appendix

*Witnesses**

James W. Ethington: Vice-Chairman of the Board and Chief Financial Officer of Sundstrand Corporation.

John B. Huarisa: Defendant and Chairman of the Board of Standard Kollsman Industries.

Donald E. Miller: Former Comptroller of Sundstrand Corporation.

Bruce F. Olson: Chairman of the Board and Chief Executive Officer of Sundstrand Corporation.

Charles E. Pitte, Jr.: Partner, Schiff, Hardin, Waite, Dorschel & Britton law firm.

Ted L. Ross: Secretary and Comptroller of Sundstrand Corporation.

Carl L. Sadler: President and Chief Operations Officer of Sundstrand Corporation.

Louis H. Schuette: Chairman of the Board and Chairman of the Executive Committee of Sundstrand Corporation.

Attorneys

Paul E. Freehling: Counsel for defendants Sun Chemical Corporation and the Estate of John B. Huarisa.

Donald R. Harris: Counsel for defendant Henry W. Meers.

W. Donald McSweeney: Counsel for plaintiff Sundstrand Corporation.

William A. Montgomery: Counsel for plaintiff Sundstrand Corporation.

* The positions designated are those that were held at the time of the testimony of the witness in question.

B. Citations in the Court's Original Footnote 35

Trial Transcript, p. 131 (James W. Ethington direct)

don't know what that is.

Mr. Dean Cameron from Schiff, Hardin came over and discussed the possibilities if Sundstrand bought those shares of stock.

I stated that Sundstrand would only be willing to buy these shares of stock if I thought a merger was going to take place.

At that time I asked Mr. Huarisa if the earnings projections that he had given us still looked good and he stated "Yes," both for 1968 and 1969 and I then said that I would call my office and see if they would be interested in buying this block of stock in order that we might proceed with the merger.

I called—

Q. Well, excuse me, if I might interrupt. Now, did that, did that occur in this meeting?

A. Yes, it did.

Q. Oh, okay. Go ahead.

A. The Pope, Ballard firm connected a line to me, and I don't know if anybody else was in the room or not, but I did call our Rockford office and I talked to Mr. Olson and Mr. Schuette and Mr. Sadler on the telephone and told them that this—

THE COURT: Well, not the conversation.

MR. MC SWEENEY: No, no.

Trial Transcript, pp. 165-167 (James W. Ethington direct)

801(d)(1)(a), statements inconsistent with his testimony. I will have to go back and check.

THE COURT: I will take a look at it.

MR. MC SWEENEY: It was not with respect to 801 (d)(b) which we are talking about.

THE COURT: Well, I would prefer to take a look at it myself.

MR. MC SWEENEY: Sure. Yes, sir.

THE COURT: All right. Let's go on.

MR. MC SWEENEY: All right.

BY MR. MC SWEENEY:

Q. Now, after this meeting about which you have testified at the conclusion yesterday, which was on or about January 23, 1969, when did you next have, if you did, any contact with anyone representing SKI concerning this entire matter?

A. Some time around the 9th or 10th of February in 1969.

Q. And where did that—was that a person-to-person meeting?

A. I made a telephone call to Mr. Huarisa asking if I could have a meeting with him and with Mr. Pitte, who is our legal counsel from Schiff, Hardin, and Mr. Huarisa stated that he would be glad to meet with me and we made a date at the Chicago Club, I believe, for February 10th, 1969.

Q. All right, sir. Who was present at that meeting—you made a date and then you had the meeting, is that right?

A. Yes.

Q. All right. Fine. Who was present?

A. Mr. Huarisa was present and Mr. Pitte and myself.

Q. And what was said by those present at that meeting, sir?

MR. HARRIS: Your Honor, I would object to that question as calling for hearsay as to Mr. Meers. I think that that is not quite in the category of the type of hearsay evidence which the Court admitted conditionally.

THE COURT: Well, if there is a so-called conspiracy and the conspiracy is still in existence—I will show your objection and I will conditionally admit it on the same basis that I have been admitting the other evidence, but I will show your objection.

MR. HARRIS: Thank you, your Honor.

THE COURT: Go ahead.

BY MR. MC SWEENEY:

Q. The Court said you may answer.

THE COURT: You may answer.

THE WITNESS: Thank you.

BY THE WITNESS:

A. I asked—I told Mr. Huarisa that the purpose of my being there was to find out what was being done on Standard Kollsman merging into another company.

I also stated to him that Sundstrand would cooperate in any merger that he might come up with.

I also stated to him that I was concerned about the disposing of the Sundstrand—of the Standard Kollsman stock that we had in our possession.

Mr. Huarisa stated that he was working on a number of acquisitions and that Mr. Meers was also working on a number and that he would be glad to guarantee an amount of money that would take Sundstrand out of this.

Mr. Pitte then said that he would draw up a document and summarize our conversation and send it to Mr. Huarisa's lawyer at Pope, Ballard.

Q. Is there anything more of that meeting that you recall, sir?

A. I can't recall anything right at this minute.

Q. All right.

Now, I show you a document which has been marked Plaintiff's Exhibit 5, purporting to be a letter, or a copy of a

Trial Transcript, pp. 484-487

(Carl L. Sadler cross-examination)

going to go ahead with the purchase of the Burke stock?" Do you remember that?

MR. MONTGOMERY: Your Honor, I object. There has been no time fixed as to when Mr. Sadler came back from vacation.

THE COURT: Well, he can ask him if he ever asked them. Then he can fix the time.

Was that question ever asked: "What are you going to do about it?"

MR. FREEHLING: All right.

BY MR. FREEHLING:

Q. Mr. Sadler, did you ever ask Mr. Ethington: "Are you going to go ahead and purchase the Burke stock?"

A. I would presume I probably asked him that some time or other.

Q. That was in early February 1969, was it not?

A. I am sorry. I don't know. If you have got something there that says so, why, that is fine, but I don't know at this moment. I don't remember is all I am saying.

THE COURT: Was it in February? Was it in February sometime?

THE WITNESS: I am sorry, your Honor, I don't remember the conversation. I am not saying it didn't happen. I just don't remember now.

BY MR. FREEHLING:

Q. At least it was after January 20, 1969, isn't that right?

MR. MONTGOMERY: Then I do object on the ground that this is beyond the scope of the direct examination.

THE COURT: Overruled.

BY THE WITNESS:

A. Well, if you can refresh my memory in some way, I will be glad to—

THE COURT: Well, can you place it as to whether it was after you decided not to go through with the merger? Can't you place it by that?

THE WITNESS: Would you like me to tell you what I know of the subject?

THE COURT: No.

THE WITNESS: I am sorry.

THE COURT: I think counsel is entitled to an answer.

THE WITNESS: Oh, all right.

THE COURT: As to when the conversation took place.

THE WITNESS: Well, your Honor, all I am trying to say is this particular conversation has escaped me. If somebody will refresh my memory, I will be glad to corroborate it, but right now, I just plain don't remember the subject. I am sure that at some time I was curious about whether we had a continuing legal obligation to buy the Burke stock. It might very well be that after January 20th, I may have asked Ethington if he thought that we had such an obligation, but my memory right now, I would be saying something I don't know if I said, "Yes, I did."

BY MR. FREEHLING:

Q. What did Mr. Ethington respond to you?

A. I am sorry. I don't know right now. Perhaps you can refresh my memory but I don't remember the conversation at this moment.

Q. Mr. Ethington told you that legal counsel for Sundstrand said that Sundstrand was obligated to buy this stock, isn't that right?

A. Well, if that is in my deposition, I am sure it is right, or in my earlier trial testimony, because I told the truth, but I don't remember it now. That is all. I am sorry.

I will be happy to have you read the deposition or whereever it is.

Q. You told Mr. Ethington, "Fine, I hope you peddle it to somebody," isn't that right?

A. Again, I don't honestly remember the conversation. I presume it is right based on some deposition material you have or such. That is a long time ago. I have just forgotten it.

Q. Mr. Sadler, were you asked these questions and did you give these answers at your deposition?

MR. FREEHLING: Pages 142 and continuing on to Page 143.

BY MR. FREEHLING:

Q. After you had been asked about the meetings on January 20, you were asked this question, were you not, the following questions and gave the following answers:

> "Q. Did you have any conversation with Mr. Ethington after that meeting?
>
> "A. Yes.
>
> "Q. About the Burke stock?"

Then there was some colloquy between counsel and you answered:

> "A. Yes. I remember that some time shortly after I got back from skiing, the question came up about proceeding with the purchase of the Burke stock, and I said, 'Are you going to go ahead?' He said, 'Yes, as our counsel feels we are obligated to buy the stock.' I said, 'Fine. I hope you can peddle it at a good price to somebody.' That was the sum total of it."

Were you asked those questions and did you give those answers, Mr. Sadler?

A. If my deposition says so, I absolutely did.

THE COURT: What was the date of the deposition?

Trial Transcript, pp. 625-631
(Ted L. Ross cross-examination)

Q. Do you remember what you heard at the small meeting with Mr. Ethington and Mr. Schuette?

A. I believe Mr. Sadler made a statement to the effect that it was the opinion of the team that we should not proceed with the acquisition.

Q. So you didn't hear the rest of the discussion?

A. No, I can't recall that now.

Q. Yes. Now, you were present in court at the very end of Mr. Sadler's testimony last week, were you not?

A. Yes.

Q. You heard him say that after the events of January 20, 1969, he went on a skiing vacation, do you recall that?

A. I remember him talking about the skiing vacation. I don't remember the date. I'm sorry.

Q. Do you remember—I'm sorry.

A. I don't remember the dates that occurred.

Q. And do you remember that he testified that when he returned from the skiing vacation he asked Mr. Ethington whether Sundstrand planned to buy the Burke stock, do you recall that?

A. I recall that being said. I don't know whether he said it up here or you said it when you were reading from prior testimony.

Q. And Mr. Sadler said that Mr. Ethington had responded that Sundstrand did intend to buy that stock because legal counsel feels Sundstrand was obligated to buy the stock, do you recall that?

A. Again there is confusion about who said what during that testimony.

Q. And, of course, you will recall that Sundstrand made a cash payment of about $6,300,000 on February 6, 1969, in connection with the purchase of this stock, isn't that right?

A. I am aware of that, yes.

Q. Back in those days, in January and February, 1969, your title was secretary of the corporation, isn't that right?

A. Yes.

Q. And among your duties was liaisons with Sundstrand's legal counsel, isn't that true?

A. Yes.

Q. And in addition there was an in-house attorney, Mr. Schilling, who reported to you at that time, isn't that right?

A. Yes.

Q. Mr. Ross, the fact is that Sundstrand never sought or obtained any opinion of counsel to the effect that Sundstrand was obligated to make the $6,300,000 payment in connection with the Burke stock, isn't that so?

MR. MONTGOMERY: Objection, your Honor. Irrelevant and immaterial as to whether Sundstrand ever obtained a legal opinion with reference to an obligation—

THE COURT: Well, he may ask the question whether they did.

So far as you know, did they request or receive a legal opinion?

THE WITNESS: I, your Honor—I will remind Mr. Freehling that during the time period that this was occurring I was on the East Coast a great deal of the time and Mr. Ethington dealt with Mr. Pitte directly on this transaction. They were the ones that had the meeting. I was not involved in the transaction.

BY MR. FREEHLING:

Q. Mr. Ross, do you recall—

MR. FREEHLING: Excuse me a moment, your Honor.

THE COURT: Yes.

(Brief interruption.)

BY MR. FREEHLING:

Q. Mr. Ross, I show you what has been marked as Defendant Sun-Huarisa—

THE COURT: Well, if you have an interrogatory answer why don't you read it, I mean—

MR. FREEHLING: All right.

THE COURT: Did he sign the interrogatories?

MR. FREEHLING: Well, your Honor, if I may, I will—

THE COURT: Yes.

MR. FREEHLING: —I will show Mr. Ross the Defendant Sun-Huarisa Trial Exhibit 52, purporting to be answers to interrogatories, and I will ask him whether he signed them.

THE COURT: All right. Well, if he did, you may—all right, ask him.

BY THE WITNESS:

A. (Examining documents.) That's my signature on page 96.

BY MR. FREEHLING:

Q. In response to Interrogatory No. 1-A-1, "State Each Reason Why You Make Certain Contentions. State Whether One or More Opinions of Counsel have been Obtained with Respect to Such Obligation," and so on.

You gave the following answer, did you not—

MR. MONTGOMERY: Well, your Honor, I object again as irrelevant. Whether Sundstrand obtained an opinion of counsel with reference to this question is irrelevant and immaterial here.

MR. FREEHLING: May I respond, your Honor?

MR. MONTGOMERY: This is a case which is grounded on Rule 10b-5, it does not have anything to do with a legal obligation to purchase stock.

THE COURT: Well, the question—I assume that one question involved in this case is why Sundstrand decided to proceed with the stock purchase, whether they proceeded on the basis of the representations, whether they proceeded because they thought that they had a legal obligation and had no choice except to proceed, I assume that that is—

MR. FREEHLING: That is right, your Honor, and there is a second reason: Mr. Ethington apparently told Mr. Sadler that the reason for proceeding was that there was a legal opinion.

THE COURT: Well, you may—

MR. FREEHLING: Sundstrand has stated under oath and Mr. Ross has stated under oath there was no such legal opinion. I think that goes to Mr. Ethington's credibility.

THE COURT: Well, you may proceed. I don't know what it will prove one way or the other, but go ahead.

What is the answer?

BY MR. FREEHLING:

Q. The question was, basically, whether you had obtained a legal opinion with respect to the obligation to make the $6,300,000 payment, whether you had an obligation, and, if so, on what you based that contention.

And the answer was:

> "The agreement so provides. Sundstrand relies on all the language of the agreement."

I am reading from page 5 of the answer to Interrogatory 1-A-1.

(Reading continued:)

"In addition, at the time of such sale, transfer and conveyance and at the time of such payment Sundstrand did not have knowledge that the conduct of defendant in connection with Sundstrand's purchase of SKI stock gave rise to the claim asserted by Sundstrand in this action. No opinion of counsel has been obtained with respect to such obligation."

MR. MONTGOMERY: Your Honor, I request that the balance of that answer to that interrogatory be read.

MR. FREEHLING: I will be very happy to read it.

THE COURT: Read the rest of it.

BY MR. FREEHLING:

Q. (Reading continued:)

"Counsel for Sundstrand, Schiff, Hardin, Waite, Dorschel & Britton, who have participated in various aspects of the stock purchase transaction and represent Sundstrand in this action, did not render any opinion to Sundstrand that the agreement did not obligate it to make such payment at the time such payment was made."

Did you give that answer, sign that answer—or sign the answers to the interrogatories that include that answer?

A. You have the document there. I am sure that it indicates—

THE COURT: Well, there is no question about it. Let's go on.

MR. FREEHLING: All right.

BY MR. FREEHLING:

Q. All right. Now, Mr. Ross, you attended the 1969 Standard Kollsman meeting, the annual meeting of shareholders, did you not?

A. Yes.

Q. You accompanied Mr. Ethington to that meeting, did you not?

A. Yes.

Q. And at that meeting Sundstrand voted all 223,000-some-odd shares of its Standard Kollsman stock, isn't that so?

A. Yes.

Trial Transcript, pp. 1703-1705 (Statements of Counsel)

THE COURT: Well, I will hear from Sun Chemical.

MR. HARRIS: Your Honor, since we did two things at once a little faster than I was planning on, may I hand up a 41(b) motion?

THE COURT: You may present it. Yes, you may.

MR. FREEHLING: Your Honor, I am sure it comes as no surprise that the two defendants I represent also have a 41(b) motion which I serve.

THE COURT: No.

MR. FREEHLING: Your Honor, I will be very brief. I would like to avoid repeating what Mr. Harris has said, but at the same time, I would like to speak to the motion.

Your Honor, I would like to speak in particular to two of the questions that your Honor asked yesterday. One of them actually was addressed to the plaintiff: Why did Sundstrand complete the purchase of the stock after having turned down the merger? The second question, which was the one directed at my clients: namely, explain the disparity between events in the fall of 1968 and the results of the audit in the spring of 1969.

As I say, your Honor, I am going to be very brief unless your Honor asks me to expand.

As to why Sundstrand bought that stock, we know that Sundstrand on acquisitions as small as a million dollars, which is less than 15 per cent of the size of the purchase of the Burke stock, made exhaustive examinations before committing themselves. We know that Sundstrand made an exhaustive examination of Standard Kollsman in connection with the planned merger. We know that it was on February 6 after the exhaustive examination was over that Sundstrand for the first time paid anything or did anything in connection with this acquisition of stock.

The agreement in our view committed Sundstrand to do absolutely nothing until February 6th, but whether it did or—I am sorry. It committed Sundstrand to do absolutely nothing except to reimburse Huarisa for the first $335,000 payment.

On February 6, Sundstrand had done nothing. They had not reimbursed Huarisa, they hadn't paid nothing to the Burkes.

It was at that moment, February 6, that their conduct has to be viewed. It is at that time that Sundstrand had a complete view of Standard Kollsman, a view, as Mr. Ethington told us, that had let them to call off the merger proposal basically because they had no confidence in the earnings projections of Standard Kollsman, basically because they were convinced that over $4 million of assets on the books of Standard Kollsman would not be recoverable and would have to be written off.

Your Honor, the results, as bad as they were at year-end 1968, weren't that bad. Sundstrand saw things at Standard Kollsman as being in a worse light than even Price Waterhouse.

I submit, your Honor, that what has to be viewed here in terms of so-called reliance by Sundstrand is their knowledge as of February 6th, first, because that is the first time they paid anything or did anything and, secondly, because they in fact weren't obligated to do anything at all until that date.

Now, I don't want to repeat myself and I don't want to repeat Mr. Harris. I do want to bring to your Honor's attention one matter.

THE COURT: When you talk about that date, let's go back a little ways. You are saying in effect they could have rescinded the transaction and minimized their damages perhaps, but they still were going to get caught to the extent of what, $300,000 or $400,000. What you are in effect saying to me is they at that time, if they had been misled, they shouldn't have plunged in any deeper.

Doesn't that go to the question as to the amount of damages rather than the question whether damages should be assessed?

Trial Transcript, pp. 2022-2023 (Remarks of the Court)

make a move, I think what you better do is to consider it on the basis that, well, here it is, and tender it to the plaintiffs, and they can say yes or no or they can give you some other quick response. The whole thing, you can solve it one way or the other if you are going to solve it over the weekend, it seems to me. If you come back in and tell me at 10:30 on Monday morning that you have settled it, I will be pleased. If you tell me you can't settle it, I won't be as pleased but, at the same time, we will finish up the case and then I will go to work on it.

Let me say so far as the plaintiffs are concerned, I don't profess to have my mind made up in this case. I certainly

am not going to make up my mind until the conclusion of the case, and I am not going to make up my mind then. I am going to get briefs and I am going to study it further. I have got to read some depositions. I am in no position to make a decision.

I think there are some problems in this case both ways. I have said it is a case that I thought ought to be settled. I say it because I certainly think there are some problems so far as the defense is concerned.

On the other hand, I don't think the plaintiff has an entirely open field running to early victory or something like that. There are elements besides the mere fact of the making of representations. This case has some unique features.

One unique feature is that the company turned down the merger and then proceeded to go ahead and buy the stock. I haven't made a definite conclusion as to whether or not the company was really obligated to buy it when it bought it or not, but that certainly is an arguable question as to whether you were obligated or not obligated.

I don't think you will find many cases like this. If the merger was turned down, the usual procedure would be to turn down the whole business if you could.

Now, I don't know what effect that may have on the final outcome but that certainly is an element that the plaintiff ought to consider. There ought to be some flexibility based on factors such as that. If you had just a merger case here, my life would be a lot simpler, but you haven't got that. You turned away from that and you turned away from it after making some investigation, a pretty complete investigation.

But there is a whole raft of arguments that somebody is going to have to make a decision about. I don't know. When a case is tried before a judge, I

Trial Transcript, pp. 2420-2423 (Statements of Counsel)

MR. MC SWEENEY: Well, our position is that, first, we had a contract in which we would have been liable for the entire amount.

THE COURT: Well, tell me what provision—what is the provision in the contract that requires you to complete the purchase?

MR. MC SWEENEY: All right.

THE COURT: Do you want to refer to that?

MR. MC SWEENEY: Paragraph 1.

THE COURT: What does it say?

MR. MC SWEENEY: That Huarisa sells, conveys to us.

THE COURT: Yes, and what do you agree?

MR. MC SWEENEY: Subject to the payment of the unpaid balance of $6 million.

THE COURT: Well, do you agree to pay it?

MR. MC SWEENEY: We hadn't paid it by then but we were bound to pay it.

THE COURT: Under what language?

MR. MC SWEENEY: We rely on the entire agreement, specifically Paragraph 1.

He came forward with the stock, the 223,000 shares.

THE COURT: Well, actually you consummated the deal. My question is, were you obligated to consummate the deal?

MR. MC SWEENEY: Our position is we were obligated to consummate the deal.

THE COURT: All right.

MR. MC SWEENEY: Certainly, alternatively, we would have been liable for the $335,000 he had paid out for whatever consequential damages occurred as a result.

THE COURT: Well, I don't have any problem about getting your money back.

MR. MC SWEENEY: We were subject to whatever damages it would cause us as a company and our reputation for not going through with the contract.

Your Honor, the additional factor is we did not have to have a legal obligation to buy the stock.

THE COURT: Well, tell me about that.

MR. MC SWEENEY: Well, we had what we thought at least was a legal obligation and a moral obligation. Since we did not know of the fraud, even though we didn't want to go into a $100 million merger for many reasons, we still could buy the stock whether or not we were legally obligated.

Now, I submit if we had known then in February and March what we knew after a year or two of discovery in this case, we would not have done it. But whether or not we had a legal obligation even, we were entitled to buy the stock because we didn't know of the true condition of the company.

We knew enough to know that we didn't want a merger and involve our company with theirs for the various reasons that were given, those three reasons, but even if your Honor should decide there wasn't a legal obligation to go forward, there was no legal obligation on us to stop.

Moreover, as we have put in our case at length, the misrepresentations to us continued even after January 9th.

THE COURT: I understand that. On that point, perhaps Mr. Montgomery can answer this question. I think he handled most of this in putting in proofs in this case.

What I would like to focus on at this point is what were the particular facts in the Burke and the Ernst reports that if they had been called to the attention of Sundstrand prior to the Huarisa deal, they would have discouraged the making of any deal? The particular facts in the Burke and Ernst reports that would have in effect queered the whole deal right at that point.

MR. MONTGOMERY: Well, first of all, your Honor, the existence of the controversy and the existence of the communications by Burke and those in the Ernst & Ernst letter to the board of directors by and at the instigation of a member of the board of directors and major stockholder of the company is in itself a material fact that should have been disclosed and would have made a difference in this transaction. In fact, in their entirety—that is to say, without taking the particular contentions that Mr. Burke or Ernst & Ernst advanced in these documents—

THE COURT: They should have said, "We have got a dissident stockholder and we have been having some trouble with him for about six months, and he has gone to the SEC, and we have had some problems with him but we think he is clear off base and we have got the matter settled" or something?

Trial Transcript, pp. 2516-2519 (Statements of Counsel)

The record shows further there was a third meeting on January 20, and I am talking about before they start talking to Standard Kollsman. Now, this is strictly in Rockford, Illinois.

Ethington and Schuette discussed how to handle this problem they were now faced with, namely, the team's recommendation that the merger should be called off, and Ethington and Schuette's conclusion was that the merger should be called off. They had their third discussion. And, again, the earnings problem, the writeoff problem, the preproduction costs problem, was discussed.

Finally, then, as your Honor will recall, there was an evening meeting on January 20 and again the three factors were laid out, followed by another meeting on January 22 when once again the three factors were laid out.

Now, those matters, your Honor, that I have just been discussing are facts which Sundstrand learned after January 6th when the meeting was held at Pope, Ballard that led up to the January 9th agreement, but before February 6th when Sundstrand made its $6 million-plus investment. So, that is Item No. 1 with a big asterisk next to it as to what Sundstrand knew on February 6th that they did not know on January 9th.

THE COURT: They knew enough that they didn't want to go through a merger but they apparently didn't know enough to convince them that they didn't want to buy the stock.

MR. FREEHLING: Well, your Honor, I would remind your Honor of another thing that happened between January 9 and February 6th, or really two things that happened: Mr. Ethington and Mr. Sadler, two of the top officers of the company, had dumped their own stock. They did it before—their own Standard Kollsman stock—they did that before the merger was called off. So, they had apparently learned something between the time that they bought and the time that they sold that made them think that the stock wasn't a very good investment.

THE COURT: But let me ask this question: Even though there was no legal obligation, perhaps, to purchase this stock, I mean, if I reach that conclusion, I suppose that the argument can be made that insofar as Sundstrand was concerned, they had made a deal, in effect had made a deal —at the time that they made it they thought that they were going to go through with it, and they had made a deal with Huarisa, and I recall reading something in the testimony to the effect that at that time, at the time that the merger was being called off, he assured Huarisa that they would go through with it. So, they apparently felt some kind of, perhaps some kind of an obligation.

Now, why in the world would they be selling their own stock and then keeping $6 million worth of stock for their company? I mean, how would you explain something like that?

MR. FREEHLING: Well, your Honor—

THE COURT: I mean, are you saying that they were worried about the situation to the point where they got rid of a few shares of stock and then took $6 million worth and put it in their company—they were going to get hurt by that, weren't they, if it was bad stock?

MR. FREEHLING: Your Honor, unfortunately I don't believe that we know why Sundstrand went ahead and invested the $6 million. We know that they did it but we don't know why.

I could surmise, if your Honor would want me to, but it won't be based on anything in the record.

Obviously, Mr. Ethington felt personal discomfort at holding Standard Kollsman's shares in the second week of January in 1969 but he didn't feel personal discomfort, or

even corporate discomfort, about buying stock in the first week of February 1969. But as to why he felt the discomfort on the one hand the comfort on the other, I can only speculate because there is nothing in the record.

I think that what he believed in February was that somebody was going to merge with Standard Kollsman; if it wasn't Sundstrand it was going to be Sun Chemical or Riker Video, or maybe some company whose name had not yet surfaced, but somebody was going to merge, and that he would probably, that is, Sundstrand, would probably get out of this investment without a loss, but that's something we don't know. That's something that is not in the record.

THE COURT: You think that the effect of any misrepresentations that may have been made or any omissions that may have been omitted more or less had all worn off by that time, I mean, by the time that they decided not to go through with the merger? I mean, they were told a lot of things during the course of the meetings with Huarisa and some material that they wanted to get they were not able to get, isn't that true?

I mean, some of the—

MR. FREEHLING: Oh, no, your Honor, I think on the contrary.

THE COURT: I mean, some of the—what is it, the KIC material?

MR. FREEHLING: I'm sorry?

THE COURT: KIC—what is "KIC"?

MR. FREEHLING: Kollsman Instrument Corporation.

THE COURT: Well, I mean, not KIC, the Avionic material.

MR. FREEHLING: Your Honor, I think that the record establishes that anything and everything that Sundstrand asked for they received.

Trial Transcript, pp. 2620-2622 (Statements of Counsel)

to do with a merger that was never consummated. What you are trying to hold him for is a sale that he didn't even know was going to take place until a day or so before it happened.

MR. MONTGOMERY: That is true, your Honor, but it is irrelevant to this case. As the Court has said, we could have gone out and bought it in the open market for that matter.

You know, it was entirely reasonable that our having shown in interest in this company, we might buy stock.

THE COURT: Let's get back—I think we better get down to some more basic—well, these are all basic, but I will let you address yourself to the question—

First of all, you better spend some time with me, if you want to—I have already indicated that I am at least presently of the view that there are two relevant dates to consider. You are going to in effect be presented with the problem of what position your client was in when he turned over or in effect paid that balance of $6,300,000.

At that time the picture was not the same picture that he had back in January. At that time, I mean, Sundstrand knew a whole lot that they didn't know at the time they got themselves involved in the deal.

I read that document over a half a dozen times and I can't find any legal obligation in the document. I think Sundstrand had decided they were through with the merger, they could have walked off from the whole deal. But they

decide ahead and purchase the rest of the stock and put up six million dollars. They are entitled to at least show me what representations or what affected them in making that purchase, whether it was just a business judgment or speculation or whether they were relying on some facts that they had received in connection with their investigation of the merger and still thought they had some good stock they were buying and went through with the deal on that basis. I can't find and I don't think I am going to find that they had any legal obligation.

THE COURT: They might have considered that they had a moral obligation but not a legal obligation to proceed with the purchase.

MR. MONTGOMERY: Well, your Honor, I can assure you that rightly or wrongly Sundstrand considered it had a legal obligation and it also considered that it had a moral obligation—

THE COURT: That doesn't help them if they thought they had a legal one, I mean, I think that they are in the same position that anyone would have been—I mean, as of that time; they got themselves involved, they had a decision to make. "Shall we go through with it?" And they apparently made the decision to go through with it. But so far as the fact that they were compelled to do it, I can't find that in the language of the agreement.

MR. MONTGOMERY: I don't think that's the issue, your Honor. I think this is a red herring in this case, whether they had a—I mean, you know, my position is that they had a legal obligation.

THE COURT: All right.

MR. MONTGOMERY: And I don't back off from that. But I don't think that's the pertinent question.

THE COURT: That doesn't decide the case, I will agree with that.

MR. MONTGOMERY: That is right. That's not a key question here, and it doesn't—it also doesn't then reduce it to the simplest question, "Well, you made an investment on January 9 and you made another investment on February 6th." That's not what we

Trial Transcript, pp. 2624-2627 (Statements of Counsel)

the agreement here is the voidance of deal. You know, they contend we didn't buy it from Huarisa because the money went to the Burkes.

THE COURT: I don't have any problem on that, I think you did buy it from Huarisa.

MR. MONTGOMERY: Okay. Well, we didn't know, if we didn't go through with the deal we didn't know what Huarisa might sue us for and we had made an agreement with Huarisa which we—we couldn't just back off with it, one we couldn't back off from, without having a harm to our reputation as a reputable business concern.

We had no knowledge that there had been any fraud practiced upon us. And another fact, it seems to me that is worthy of consideration by the Court is a matter that we had paid or committed, in effect paid, committed to pay, this $335,000 to Huarisa, which was, at a minimum, an impediment to our abandoning the transaction.

I refer the Court to a case which we had cited in the first trial. I don't think that it was cited in this brief, but it is Bershad vs. McDonough, 28 F.2d 693. It is a Seventh Circuit decision in 1970. It is a case under Section 16(b) not under 10b5.

But there was a very similar situation there in terms of the kind of transaction that was in question. And the Court said on Page 698:

> "The circumstances of the transactions clearly indicate that the stock was effectively transferred for all practical purposes long before the exercise of the option. The $350,000 binder ostensibly paid for the option represented over 14 per cent of the total purchase price of the stock. Granting the magnitude of the sale contemplated, the size of the initial commitment strongly suggests that it was not just a binder. The extent of that payment represented, if not the exercise of the option, a significant return to the abandonment of the contemplated sale."

So, I don't think that—

THE COURT: Well, I suppose that you have got that argument here, but the fact remains that so far as that, what started out to be an option, at least, as between the Burkes and whoever was exercising the option, nothing could have happened so far as the Burkes were concerned; they would have been—they would have had $334,000 but they would have kept the stock and you would have been out of the picture.

MR. MONTGOMERY: Well, we had our agreement with Huarisa.

THE COURT: I know it.

Well, then the question is, did Huarisa have you in a situation under the terms of that agreement where you were not complying with the agreement; you never agreed in that agreement with him that you were purchasing the stock, that you would purchase the stock. He was transferring it to you, subject to.

MR. MONTGOMERY: Well, your Honor, you know, it's easy, really, to evaluate the transaction now in those

terms, and I suppose you could have—you could have, maybe, a law school exercise on this, but we are really talking about—we are talking about the activities of parties who actually did this.

THE COURT: Well, as I said a while ago, they may have felt legally obligated, rightly or wrongly, but the fact is that they put the money up in February and I think that you are going to have to judge the transaction as to whether or not they were, in effect, defrauded in some one way or another on the basis of the conditions that existed at the time that they paid over the $6 million.

MR. MONTGOMERY: Well, one of the conditions that existed was that—

THE COURT: Let's take it from there.

MR. MONTGOMERY: One of the conditions that existed was this agreement—

THE COURT: Take it from there.

MR. MONTGOMERY:—and the very fact of this agreement was what they were relying on, one of the things, one of the many things that they were relying on at the time that they made the payment, and in the context of this case the agreement, at a minimum, is important from the point of view of their reliance, their belief that they had an obligation, legal, moral, personal to Mr. Huarisa, whatever, to go ahead and consummate this transaction.

You recall, your Honor mentioned this morning, Mr. Huarisa—or Mr. Ethington—said to Mr. Huarisa at the end of the January 22nd meeting, "We are going to honor our commitment."

Huarisa didn't say, "You don't have any commitment to me." He was told by Ethington then.

THE COURT: What was his interest at that time? I mean, Huarisa wasn't going to—he had lost the merger already.

MR. MONTGOMERY: Yes, he—

THE COURT: Do you think that he just wanted to get rid of the Burkes? Was that it?

MR. MONTGOMERY: He had an unfriendly merger partner in the wings if Sun Chemical got this stock and he had an investment of 172,000 shares in SKI, independent of the

Trial Transcript, pp. 2635-2638 (Statements of Counsel)

mate of 80 cents to $1.

THE COURT: Let me ask this question—I think that I know the answer without asking it, but, is there any place in any deposition or transcript or trial testimony where any explanation was made by Sundstrand as to why they determined to go ahead with the Huarisa deal after they decided that they were not going to go through with the merger? Is there any single word of testimony in the record that would show the reason for proceeding?

MR. MONTGOMERY: I don't recall any as such, your Honor, but there is testimony in the record that they thought that they had bought the stock on January 9th. There is testimony that the directors—

THE COURT: The word "commitment" is in there. Well, where is the testimony in the record that they thought that they had purchased it, the whole stock, on January 9th?

MR. MONTGOMERY: There is testimony of Mr. Schuette concerning the telephone conversation that Mr. Ethington had with the—

THE COURT: Well, at that time they thought that they had—at that time obviously they expected to go through with the deal.

MR. MONTGOMERY: That is right, but they were making the decision—they thought that they were making a decision at that time—

THE COURT: Well, they were certainly making the decision that they were going to acquire this, and—but the purpose of acquiring it was in connection with the merger.

MR. MONTGOMERY: No, but—that's true, your Honor, that's true, but what I was about to say was, Mr. Schuette testified that there was consideration given in that telephone conversation to what would happen in the event that the merger did not go through, and they evaluated this—

THE COURT: Well, you mean that Sundstrand did?

MR. MONTGOMERY: That is right. On January 6th in a telephone conversation between Mr. Ethington and Mr. Kennedy's office in Chicago and Mr. Schuette and Mr. Sadler, and I am not sure whether Mr. Olson was there, in Rockford—

THE COURT: Well, what did they say? What did they say in the event that it did not go through—

MR. MONTGOMERY: They evaluated the downside risk in the event that the merger did not go through and concluded that because, as I recall it—

THE COURT: Would you refer me to that.

MR. MONTGOMERY: Yes. Just a moment.

THE COURT: Give me the transcript on that.

(Brief interruption.)

THE COURT: Well, you can give me that later.

MR. MONTGOMERY: Okay.

THE COURT: You say they discussed it and it said—talked about the downside, and then what? What did they find out was—

MR. MONTGOMERY: Well, they decided, "Well, we will go ahead and buy the stock," because—

THE COURT: That was at what point? At what point was this?

MR. MONTGOMERY: That was in January.

THE COURT: Right at the beginning?

MR. MONTGOMERY: That was—that was in the beginning, that was on January 6th.

THE COURT: They were discussing the possibility that the merger wouldn't go through.

MR. MONTGOMERY: That is right.

THE COURT: But had they already obligated themselves at that time to buy?

MR. MONTGOMERY: They were in the process of making the decision that they would buy it. They had not yet obligated themselves to buy it. This was a discussion concerning whether they would obligate—whether they would make that decision.

What I am saying is, it is proof of their understanding of what they were doing because they did decide to do it and then they did it. It is proof of their understanding.

It is not, as counsel suggests, a matter of Sundstrand just—a matter of why did Sundstrand do it.

As far as Sundstrand was concerned, they bought the stock on January 9th. Now, I appreciate your Honor may

have a different view as to whether they had a legal obligation to pay on February 6th but I think that the real live people who were doing this are important to consider and I think that in the context of this case more important to consider.

Deposition of John B. Huarisa, pp. 229-230

Q. Well, going back to your meeting on January 22, 1969, did Mr. Meers say anything about the write-offs?

A. No.

Q. As far as you know, he didn't say anything about anything at that meeting?

A. Well, I am sure he voiced some opinion, but I don't recall on any specific subject.

Q. Well, what was the final outcome of the meeting?

A. The final outcome of the meeting is that we would like to call it off.

Q. And that was agreed to, was it?

A. That was agreed to.

Q. And nothing was said at this meeting about the matter of the purchase of the shares of stock which were or had been owned by the Burke family?

A. As I remember, I don't know the exact words, but when the meeting broke up Mr. Ethington turned to me and said, "John, we are going to honor our commitment." Just as simple as that, and he also stated that he was going to return all the documents that he received from us.

Q. Okay, anything else?

A. And we would work out a joint announcement.

Q. I see; and did you do that?

A. Yes.

Q. Right then did you work it out?

A. No, I think it was worked out the next day.

Q. All right; anything else said at the meeting or subsequent to the meeting on January 22nd?

A. Not that I can remember.

Q. What did you say when Mr. Ethington said to you he was going to honor his agreement?

A. I didn't say anything.

Q. All right.

Now, after January 22nd, when was the next time you had anything to do with the—had any discussion with anyone concerning the Sundstrand matter?

A. Well, we probably discussed it with a lot of people in our organization, what was the cause, what was the—but nothing that I can say specific.

Q. When was the next time you had a meeting or a conversation with any representative of Sundstrand?

A. I had a luncheon date with Mr. Ethington and

Sun-Huarisa Exhibit 52: Plaintiff's Answers to First Set of Interrogatories of Defendants Standard Kollsman Industries, Inc. and John B. Huarisa, Interrogatory No. 1

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

SUNDSTRAND CORPORATION, a Delaware corporation, *Plaintiff*, *vs.* STANDARD KOLLSMAN INDUSTRIES, INC., an Illinois corporation, JOHN B. HUARISA and HENRY W. MEERS, *Defendants.*	Civil Action No. 69 C 1660

PLAINTIFF'S ANSWERS TO FIRST SET OF INTERROGATORIES OF DEFENDANTS STANDARD KOLLSMAN INDUSTRIES, INC. AND JOHN B. HUARISA

Plaintiff, Sundstrand Corporation ("Sundstrand"), answers the First Set of Interrogatories of Defendants Standard Kollsman Industries, Inc ("SKI") and John B. Huarisa, as follows:

Where the answer to any of the following Interrogatories requires the identification of persons or documents, the identity of such persons, who are referred to only by surname in the text of the answer, is set forth in Exhibit A hereto, and the identity of such documents, which are referred to only by deposition exhibit number or other numerical identification in the text of the answer, is set forth in Exhibit B hereto.

Interrogatory No. 1

Referring to the allegations of paragraph 6 of the complaint, relating to (a) the agreement executed January 9, 1969, (b) the transfer of 5,686 shares of Sundstrand common stock, and (c) the payment of $6,360,915,

(a) State whether you contend that such agreement obligated Sundstrand to pay such $6,360,915 and/or to transfer such 5,686 shares of stock and, if so,

(i) State each reason why you so contend (including all language of such agreement on which you rely to support such contention), state whether one or more opinions of counsel have been obtained with respect to such obligation (if so, separately for each such opinion of counsel, state whether it was in writing—in which case identify it—or was verbal—in which case identify the person or persons who expressed it—, state the date, place and circumstances of its being expressed, and identify each person who was present when it was expressed);

(ii) State the last date or dates by which you contend Sundstrand was obligated to make any part or all of such payment of $6,360,915, state each reason why you so contend (including all language of such agreement on which you rely to support your contention), and, if one or more of such last dates for payment are later than the date Sundstrand did pay such sum, state each reason why payment was made earlier than the last date for making payment;

(b) State whether the payment of $6,360,915 was made by check or checks drawn by Sundstrand and, if so, separately for each such check,

(i) State its date, amount, and the name of each payee and each endorser;

(ii) Identify each person who gave instructions to one or more Sundstrand officers, directors or employees relating to drawing such check or checks and,

separately for each such person, state the date, place, and circumstances of such instructions being given, identify each person to whom they were given and each other person present, and identify each documents relating or pertaining, directly or indirectly, thereto.

Answer to Interrogatory No. 1.

(a) As to the payment of $6,360,915, yes. The 5,686 shares of stock were sold, transferred and conveyed to Huarisa by the terms of the Agreement (paragraph 2).

(i) The Agreement so provides; Sundstrand relies on all the language of the Agreement. In addition, at the time of such sale, transfer and conveyance, and at the time of such payment, Sundstrand did not have knowledge that the conduct of defendants in connection with Sundstrand's purchase of SKI stock gave rise to the claim asserted by Sundstrand in this action. No opinion of counsel has been obtained with respect to such obligation. Counsel for Sundstrand, Schiff Hardin Waite Dorschel & Britton, who have participated in various aspects of the stock purchase transaction and represent Sundstrand in this action, did not render any opinion to Sundstrand that the Agreement did not obligate it to make such payment at the time such payment was made.

(ii) The payment of $6,360,915 was made by Sundstrand in accordance with the terms of the Agreement. Sundstrand has no contention as to the last date or dates by which it was obligated to make any part or all of such payment.

(b) (i) The payment of $6,360,915 was made by a cashier's check drawn on the First National Bank of Chicago, a copy of a facsimile of which is attached hereto as Exhibit C.

(ii) On or about February 3, 4 or 5, 1969, in one or more telephone conversations between Pitte, who was in Chicago, and Ethington, who was in Rockford, Illi-

nois, Pitte related to Ethington instructions relating to the drawing of such check which he had received from Hart of Pope, Ballard, Kennedy, Shepard & Fowle, counsel for Huarisa. No other person was present on either side of the telephone conversation between Ethington and Pitte.

On or about February 5, 1969, in a conversation at the Sundstrand corporate offices in Rockford, Illinois, Ethington gave instructions to Swanson relating to the drawing of such check. No other person was present at that time. Documents related thereto are Defendants' Deposition Exhibit Nos. 122 and 122-A.

I, Ted L. Ross, being duly sworn upon oath, depose and say that I am Secretary of Sundstrand Corporation, plaintiff in this cause; that the foregoing answers to interrogatories have been prepared by me and by counsel for Sundstrand; that such answers are based in part upon my own personal knowledge, in part upon information assembled from Sundstrand's records, in part upon conversations between myself or counsel for Sundstrand with certain of its officers and employees, and in part upon the deposition testimony and exhibits and other documents in this cause; and that such answers are true and correct to the best of my knowledge, information and belief.

/s/ Ted L. Ross
Ted L. Ross

Subscribed and sworn to
before me this 30th day
of October, 1970.

/s/ Judith A. Barr
Notary Public

My Commission Expires Dec. 14, 1971

IV. CITATIONS ADDED TO FOOTNOTE 35 BY THE COURT'S ORDER OF MAY 18, 1977

Brief of Appellee Sundstrand Corporation (August 27, 1976), p. 77

stituting the violation of Rule 10b-5 (Mem.Op. 71-72, App. 173-74). Jacobs, *The Impact of Rule 10b-5* § 40.04, p. 2-79 (1974).

IV. DEFENDANTS' ARGUMENTS ON THE ISSUES OF DAMAGES AND INTEREST ARE WITHOUT MERIT

Although Sundstrand had sought judgment for a principal amount ranging from approximately $6,700,000 to $6,200,000, based on alternative theories of relief,* the District Court awarded damages in the principal amount of $4,434,786, representing the difference between the price paid by Sundstrand and the Court's determination of the actual value of the acquired stock, plus interest from February 6, 1969 (Mem.Op. 75-76, App. 177-78). Defendants make a shot-gun attack on the District Court's findings concerning damages and interest, but each shot misses the target.

A. Sundstrand's Recovery Is Not Limited to the Amount Paid on January 9, 1969 or the Amount Due on February 6, 1969

The initial argument made by all defendants, that at most defendants are liable for inducing Sundstrand's initial payment of $334,785 (Sun-Huarisa Br. 55-56; Meers Br. 71), is merely a restatement of their erroneous argument that plaintiff failed to prove causation (*see* Point II-D, *supra,* pp. 61-64). Meers also argues that, in any event, on February 6, 1969, only partial payment was due under any reading of

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* Sundstrand sought rescission of its purchase of SKI stock (for which it had paid $6,695,700) or, in the alternative, the difference between the price paid for the stock and the amount for which the stock could have been sold at the time of the merger of SKI into Sun Chemical, with an appropriate discount because the stock was restricted. *See* Plaintiff's Answers and Objections to First Set of Interrogatories of Defendants Sun Chemical Corporation and John B. Huarisa to Plaintiff Sundstrand Corporation, No. 1(d), Record No. 464.

Petition for Rehearing and Suggestion of Rehearing en Banc on Behalf of Appellee Sundstrand Corporation (March 29, 1977), p. 10

(Slip Op. 27-28 and n. 35), was in the face of the District Court's findings on causation and its repeated, explicit rejection of defendants' arguments. In so ruling, this Court both expressly relied upon material not in the trial record (*see* Part IV, *infra*) and failed to adhere to the requirements of Rule 52(a), Fed.R.Civ.P., that "findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses."

The District Court held that Sundstrand consummated the purchase on February 6, 1969 because it relied upon the misrepresentations and omissions made by the defendants.[8] The District Court also explicitly rejected the defendants' contention that by February 6, 1969, Sundstrand had knowledge of the omitted or misrepresented facts. Pertinent findings of the District Court include both those pertaining to defendants misrepresentations and omissions (Mem. Op. 29-61, App. 131-63) and the following findings:

> Though defendants Sun Chemical and Huarisa claim that Sundstrand had full access to all relevant sources of information during the survey [of SKI in January, 1969], such was not the case, particularly with

[8] The District Court did not conclude that Sundstrand "completed the transaction for investment purposes" (Slip Op. 27); it merely held that Sundstrand was entitled to "its rights as an investor." (Mem. Op. 28, App. 130) The motive for making a purchase of securities is irrelevant under Rule 10b-5; the issues are reliance and causation. In any event, this Court's statement that any District Court finding that Sundstrand was investing in SKI stock was *sua sponte* (Slip Op. 27) is incorrect. Both counsel for Sundstrand (Tr. 2421-23) and counsel for Sun and Huarisa (Tr. 2516-19) referred to this theory in argument. Moreover, notwithstanding the Court's assertion that Sundstrand advanced a causation theory "for the first time in this Court" (Slip Op. 27), plaintiff has for years consistently contended that "[d]efendants are liable to Sundstrand even if the stock purchase did not occur until February 6, 1969." (Plaintiff's Trial Brief, p. 94, filed September 10, 1975, Record No. 615(a))

respect to financial information. (Mem. Op 22, App. 124; Venner Dep. 18-20, 32-35; Katz Dep. 212-13; Nichinson Dep. 175-78, 252, 620-22; Ross Tr. 511-12, 537-38, 641-42)

* * *

. . . Between January 9 and the purchase of the 223,190 shares of SKI stock by Sundstrand on February 6, Sundstrand conducted an investigation of SKI, described above. This investigation, however, did not cure the previous misrepresentations and omissions. In fact,

V. ADDITIONAL REFERENCES TO THE TRIAL RECORD CITED IN PETITION OF SUNDSTRAND CORPORATION

Deposition of Louis H. Schuette, pp. 330-333

Q. Did Mr. Ethington in the period between January 6 and February 6 ever discuss with you whether the Standard Kollsman stock would be a good investment for Sundstrand?

MR. MONTGOMERY: Would you read that back?

(Question read by the reporter.)

MR. MONTGOMERY: Is this including the conversation of January 6?

MR. FREEHLING: Oh, we will exclude the conversation of January 6.

BY THE WITNESS:

Q. Yes. Generally I think I have already testified as to the price earnings ratio of people in the electronics industry and if the projected earnings were there what the stock would be worth. We were quite knowledgeable as a result of having negotiated with Mr. Meers, that there were a number of other companies interested in Standard Kollsman and we did not feel that it was too bad an investment if this was the situation.

Q. Did there come a time when you had some doubts about the ability of Standard Kollsman to project its earnings?

A. I sure did.

Q. And that was in mid to late January 1969?

A. That was our own assessment. The published information came out in March or April.

Q. Was there any discussion with Mr. Ethington after you reached the conclusion that you did not have the utmost confidence in Standard Kollsman's projections, but

prior to February 6 as to whether the Standard Kollsman stock would be a good investment?

A. I don't—repeat that question. I got lost in that one.

(Question read by the reporter.)

BY THE WITNESS:

A. Yes.

Q. What was said by you and what was said by Mr. Ethington in that conversation?

A. We again went through our same reasoning, that maybe we were wrong. We were not the greatest people in the world. Maybe he was right. Because he continued to emphasize even in the meeting of January 22nd that we were wrong and that he was right in what he had projected. And if he were right and if they had all of these other people that were potential merger partners, it must have been a good investment.

Q. A good investment for Sundstrand?

A. Yes.

Q. Was that a single conversation with Mr. Ethington?

A. No, that was a mutiple conversation.

Q. And all of those were after January 22nd but prior to February 6th, is that right?

A. Continuous discussion, yes. There were a number of them later.

Q. There were a number of those conversations between the period of January 22nd?

A. Between Mr. Ethington and I, yes. I have already testified to that three times.

Q. Did you discuss the subject of whether the Sundstrand stock—the Standard Kollsman stock would be a good investment for Sundstrand between the period January 22 and February 6 with anyone other than Mr. Ethington?

A. With Mr. Ross, yes.

Q. What did Mr. Ross say?

A. He was quite aware of our reasoning and he did concur in it.

Deposition of Louis H. Schuette, pp. 336-337

Q. Then we can take it that on February 6 you still believed it was a good investment, is that right?

A. That is right.

Q. Now did your decision sometime in January change? You still held on February 6 that the stock was a good investment for Sundstrand. Was that decision based in any way on the projection of 1968 earnings of Standard Kollsman?

MR. MONTGOMERY: You say decision. You are using the word "decision." I don't think he said he made a decision.

BY MR. FREEHLING:

Q. His opinion.

A. The opinion was based on our original discussion with Mr. Huarisa they had made 85 cents the third quarter. By the third quarter of 1968 Kollsman Instruments had turned into the black and they expected an increase in earnings for 1968. And their projections into 1969 on the basis of which we were to negotiate was originally stated as about $2.41. It was later modified to about $2.13 or $2.14, somewhere in there. So yes, it did have some influencing factor when these earnings came out.

Trial Transcript, pp. 749-752
(Donald E. Miller cross-examination)

Q. Now, Mr. Miller, about February 1, 1969, you first heard about Sundstrand purchasing some Standard Kollsman stock as opposed to merging with the whole company or acquiring the whole company, isn't that true?

A. Yes.

Q. You heard about it from a Mr. Isaacson, did you not?

A. Yes.

Q. Who was Mr. Isaacson?

A. Mr. Isaacson was in charge of the corporate accounting at Sundstrand at that time.

Q. And this conversation was shortly before Sundstrand paid 6,300,000-some-odd dollars, isn't that true?

A. True.

Q. And you had a conversation with Mr. Ethington about that purchase at the same time, at about the same time as your conversation with Mr. Isaacson, isn't that so?

A. Some time afterwards, yes.

Q. But before the money was paid, isn't that right?

A. I don't think so. It may have been.

Q. And you asked Mr. Ethington why Sundstrand would want to buy the Standard Kollsman stock after having decided not to acquire Standard Kollsman, isn't that right?

A. Yes.

Q. And Mr. Ethington explained to you that there was an agreement to buy shares of Standard Kollsman because Mr. Huarisa had a first call or option on the shares and

had been unable to come up with that much money, isn't that right?

A. Yes.

Q. And Mr. Ethington told you that he thought that the stock would be a good investment, even at $1.50 per share projected earnings for 1969, isn't that so?

A. Yes.

Q. He told you that he thought that this purchase, the purchase of this stock, would be a good investment because there were other people interested in merging with Standard Kollsman and because their projected earnings were considerably higher in 1969 than in 1968, isn't that so?

A. It sounds right.

THE COURT: Who was it who said that?

MR. FREEHLING: Sir?

THE COURT: Who was the other party to the conversation?

MR. FREEHLING: This was a conversation—

BY MR. FREEHLING:

Q. This was a conversation, was it not, Mr. Miller, between you and Mr. Ethington, the president of Sundstrand Corporation?

A. That is right.

No. 77-255

In the
Supreme Court of the United States

October Term, 197.

SUNDSTRAND CORPORATION,
Petitioner,

vs.

SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., EXECUTORS OF THE ESTATE OF JOHN B. HUARISA,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

BRIEF OF RESPONDENTS IN OPPOSITION

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In The
SUPREME COURT OF THE UNITED STATES
October Term, 1977

No. 77-255

SUNDSTRAND CORPORATION,

Petitioner,

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SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., EXECUTORS OF THE ESTATE OF JOHN B. HUARISA,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

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BRIEF OF RESPONDENTS IN OPPOSITION

QUESTIONS PRESENTED

Sundstrand presents questions for review (Pet. p. 3) which are illusory and, in reality, not presented in this case at all. As for question one, we are not dealing with a plaintiff who bought stock on the basis of concurrent causes but with a plaintiff who purchased stock solely because of a mistake of law. As for question two, we are not dealing with a plaintiff claimed to have acted negli-

gently, but with a plaintiff who has insisted it purchased stock because it was obligated to purchase it. As for question three, the Court of Appeals did not make an "independent study" of material not in the trial record so as to make findings contrary to the findings of the district court. The Court of Appeals, almost in disbelief, simply sought confirmation in the record on appeal that Sundstrand actually bought the Burke stock because it thought it was obliged to, and not for some other reason.

In reality, the only question presented by the Sundstrand Petition for Certiorari is whether the Court of Appeals decided this case correctly under all the circumstances, which of course is no basis for seeking yet another review.

STATEMENT OF THE CASE

Sundstrand's statement of the case is incomplete and in important respects unsupported by the record.

From the outset of this litigation Sundstrand sought to prove that on January 9, 1969, in the midst of merger negotiations with SKI, Sundstrand purchased 223,190 shares of SKI stock so as to prevent these shares from falling into unfriendly hands before Sundstrand had an opportunity to complete the merger negotiations. Sundstrand's case foundered, however, when all it could prove was that on January 9, 1969, it obtained an option to purchase the 223,190 shares which it need not have exercised (M.App. 17-18, 85-87); it did not buy the shares until February 6, 1969, two weeks after the merger negotiations were abandoned; on that day, without obligation, Sundstrand exercised the option, paid the $6,360,915 bal-

ance of the purchase price, and took title to the SKI shares.*

Other than to contend vigorously, but mistakenly, that it was legally committed to purchase the SKI shares on February 6, 1969, Sundstrand to this day has not explained what motivated it to buy the SKI stock when it was not obliged to buy it and when all reason for buying it had disappeared.

1. Sundstrand's Mistake of Law

Throughout the first eight years of this case, Sundstrand and its counsel have insisted unequivocally that Sundstrand was legally obligated by the January 9, 1969 agreement with Huarisa to complete the purchase of the Burke stock on February 6, 1969 (Sun App. 1-3, M. App. 17-18, 85-87). Innumerable instances where Sundstrand and its counsel have so asserted could be cited. For example, in closing argument before the district court Sundstrand's counsel, speaking for his client of course, stated flatly, "we were bound to pay" the $6,360,915 on February 6, 1969, "Our position is we were obligated to consummate the deal," "Well, your Honor, I can assure you that rightly or wrongly Sundstrand considered it had a legal obligation . . . and I don't back off from that." (S. App. 132, 133, 139).

Sadler, Sundstrand's president when he testified, conceded on cross-examination that shortly before February

* Every court that has considered the question has ruled, over Sundstrand's strenuous opposition, that Sundstrand had no obligation to purchase the Burke stock. See M. App. 17-18, 85-87, and *Sundstrand Corp.* v. *Standard Kollsman Industries, Inc.*, 488 F.2d 807, 810 (7th Cir. 1973).

6, 1969, he had asked Ethington (his predecessor as president) what Sundstrand was going to do about the Burke stock and Ethington had responded that Sundstrand was going to purchase it because "our counsel feels we are obligated to buy the stock" (S. App. 120-122).*

Actually, the record in this case supports no explanation of Sundstrand's purchase of the Burke stock other than Sundstrand's mistake of law.** Sundstrand was so committed to the proposition that it was legally bound to complete the purchase of stock on February 6, 1969, that it offered no other explanation, or evidence, as to what induced it to pay $6,360,915 to the Burke family on that date. Save for Sadler's concession on cross-examination, not a single Sundstrand witness offered a word of testi-

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* Sundstrand answered an interrogatory, "Counsel for Sundstrand . . . who have participated in various aspects of the stock purchase transaction and represent Sundstrand in this action, *did not* render any opinion to Sundstrand that the agreement *did not* obligate it to make such payment at the time payment was made." (S. App. 122-127, 150). Emphasis supplied.

** During final argument the following colloquy occurred between the district court and counsel for Sundstrand (S. App. 143):

> "THE COURT: Let me ask this question—I think I know the answer without asking it, but is there any place in any deposition or transcript or trial testimony where any explanation was made by Sundstrand as to why they determined to go ahead with the Huarisa deal after they decided they were not going to go through with merger? Is there a single word of testimony in the record that would show the reason for proceeding?
>
> MR. MONTGOMERY: I don't recall any as such, your Honor, but there is testimony in the record that they thought that they had bought the stock on January 9th. . ."

mony on the subject (either in chief or in rebuttal). Ethington testified as to what induced Sundstrand to enter into the January 9, 1969 agreement, but he said nothing at all about why Sundstrand went ahead with the purchase of the Burke stock on February 6, 1969 (Sun App. 3-6).

On its own theory of the case, then, Sundstrand's purchase of the Burke stock was induced solely by its mistaken belief that it was legally bound to make the purchase.

2. Sundstrand's Adverse Information About SKI

Even before its survey and analysis of SKI which Sundstrand undertook during mid-January 1969, and which led to termination of merger negotiations, Sundstrand knew and was concerned about the fact that SKI was carrying a substantial amount of deferred costs on its books. The subject was discussed at virtually every meeting between the parties during November and December 1968 (Sun App. 6-13). The problem of SKI's deferred costs loomed so large that Sundstrand's president at the time, Ethington, personally directed the Sundstrand survey team to investigate and report on them (Sun App. 13-14). As early as January 10, 1969, the survey team, headed by then executive vice-president Sadler, regarded the problem as serious (Sun App. 14-18). By January 13, 1969, Sadler advised Ethington that he was very pessimistic about the merger (Sun App. 18-20). On January 20, 1969, the Sundstrand management concluded that SKI was carrying in excess of $4,000,000 of deferred costs on its books which it was not likely to be able to amortize against future business (Sun App. 21-38).

On January 20, 1969, Ethington and Schuette (then Sundstrand's vice-chairman) met with Huarisa and Meers to advise them that Sundstrand had decided to terminate the merger negotiations. It was explained that Sundstrand did not foresee that SKI's huge deferred costs could be amortized against future orders. Ethington summarized the reasons he gave Huarisa and Meers for terminating the negotiations (Sun App. 39-54):

> "We talked about products and new developments and the business in general, and that we did not think we were going to get the synergism we originally thought, and there were various reasons, but *basically,* that *we did not see how the earnings were going to be met because of the tremendous write-offs that were going to be faced by Standard Kollsman in our opinion.*" (Emphasis supplied)

On January 23, 1969, it was announced that merger negotiations between Sundstrand and SKI had been terminated by mutual agreement. (Sun App. 54-55) By this time, said the Court of Appeals (M. App. 82-83, 84-85, 104, 105), Sundstrand had sufficient adverse information about SKI to know that it was not justified in paying the $6,360,915 balance of the purchase price for the Burke stock if it was not obligated to do so.

3. Sundstrand Officials Make It Clear They Personally Do Not Wish To Own SKI Stock

Ethington and Sadler had secretly purchased substantial blocks of SKI stock during late December 1968, before merger negotiations between Sundstrand and SKI were known to the public. These Sundstrand officers became so disenchanted with the financial condition of SKI during the Sundstrand survey, however, that they

promptly determined to divest themselves of their holdings of SKI stock. Ethington sold his 2,000 shares on January 14, 1969. Sadler sold 1,000 shares on January 17, 1969, and 600 shares on February 13, 1969. Plainly, neither Ethington nor Sadler wished to be owners of SKI stock. (Sun App. 56-59)

4. The Discredited Theory That, Legal Obligation Aside, Sundstrand Purchased The Burke Stock On February 6, 1969 As An Investment

In desperation, Sundstrand urged (for the first time) in the Court of Appeals that, even if it were not obligated to buy the Burke stock, it completed the transaction on February 6, 1969 for "investment" purposes. As the Court of Appeals correctly observed (M. App. 103), this theory had been superimposed on Sundstrand's case by the district court, *sua sponte.*

The investment theory, however, is inconsistent with Sundstrand's insistence that it bought the Burke stock because it was legally obligated to purchase it. The theory is inconsistent with Sundstrand's announced intention that it would be interested in acquiring the Burke stock only if the merger was to be consummated. The investment theory is inconsistent with the fact that four days after Sundstrand bought the stock it began pressing Huarisa to take the stock off its hands (M. App. 103). And, apart from those inconsistencies, there is no evidence in this record that Sundstrand made a decision to invest $6,360,915 of its corporate funds in any SKI stock, let alone the Burke stock.

Moreover, as the Court of Appeals held (M. App. 103), the notion that, despite its negative findings about SKI,

Sundstrand decided to invest more than $6 million in SKI stock in February 1969, by purchasing 233,190 shares from the Burke family at $30 per share is too farfetched to warrant serious consideration. The market price for SKI stock on February 6, 1969 was about $25 per share, $5 per share below the price of the Burke stock. Thus, "investing" in the Burke stock meant investing in 223,190 shares of SKI stock at a premium over market of more than $1,000,000. In addition, the Burke stock was unregistered, as Sundstrand knew, and therefore a subsequent sale of this SKI stock would be likely to be at a substantial discount below market (as much as 50% according to Sundstrand's expert).

Finally, this theory that apart from the proposed merger, Sundstrand may have decided to invest $6,360,915 in SKI stock, is simply not the case presented by Sundstrand in the district court.

We wind up where we began: there is no explanation in the record for Sundstrand's purchase of the Burke stock on February 6, 1969, other than Sundstrand's unfounded belief that there was a legal obligation to purchase it.

5. The Decision of the District Court

The district court concluded, correctly, that in order for a plaintiff to prevail in a Rule 10b-5 case, he must prove not only that there were material misrepresentations or omissions, but that the misrepresentations or omissions caused his injury (M. App. 57).

The district court found causation in this case on the unsupported theory that Sundstrand purchased 223,190

shares of SKI stock in reliance upon material misrepresentations and omissions of SKI and Huarisa. Specifically, the court found that, in purchasing 223,190 shares and paying the Burke family $6,360,915 on February 6, 1969, Sundstrand was relying on what had been represented to it prior to the termination of the Sundstrand-SKI merger negotiations in January 1969. The district court stated that Ethington gave direct testimony at the trial that Sundstrand relied upon SKI's and Huarisa's representations in the purchase of the Burke stock, and it stated in addition that Sundstrand's reliance was entirely reasonable (M. App. 58). Sundstrand places great weight upon these findings in its Petition to this Court.

However, these findings are clearly erroneous. They were disregarded by the Court of Appeals and should be disregarded by this Court. Ethington did testify as to what Sundstrand relied upon *in entering into the January 9, 1969* agreement (Sun App. 3-6), but neither Ethington nor any other Sundstrand witness (save Sadler) offered any testimony at all as to what Sundstrand relied upon *in purchasing the Burke stock on February 6, 1969,* or why it was purchased two weeks after the Sundstrand-SKI merger negotiations had been abandoned. Sundstrand knows full well that the foregoing findings are erroneous and were made by mistake. Sundstrand proposed these findings in conjunction with findings that Sundstrand had purchased its SKI stock on January 9, 1969. When the district court rejected that theory and found instead that Sundstrand had made its purchase on February 6, 1969, the court neglected to alter a number of related findings which were premised upon a January rather than a February, 1969 purchase, including the findings in question. The district court's mistake was brought about by Sundstrand.

There is no evidence in this case that Sundstrand was induced by defendants to purchase the Burke stock.

6. The Decision Of The Court Of Appeals

The Court of Appeals held that defendants are liable to Sundstrand for $334,785 (plus pre-judgment interest) because defendants wrongfully induced Sundstrand to enter into the January 9, 1969 agreement which obligated Sundstrand to pay $334,785 toward the purchase price of the Burke stock. The Court also held that the January 9, 1969 agreement did not require Sundstrand to pay the $6,360,915 that it paid the Burkes on February 6, 1969. Sundstrand paid that sum, the Court concluded, because it believed it was legally obligated to do so. This was a payment made under a mistake of law; it was not induced by defendants.

The determination that Sundstrand's mistake of law was the cause of its payment of $6,360,915 to the Burke family on February 6, 1969 is amply supported by the record.* Sundstrand believed it had a legal obligation to pay the $6,360,915; it has so maintained throughout this litigation. Sundstrand was wrong, however; it had no such obligation; the money was paid by mistake. Sundstrand suggests that this is a result that defendants did not seek or argue in briefs below. This is not the case; we argued to the Court of Appeals repeatedly (and to the district court, too) that there is only one rational explanation for Sundstrand's $6,360,915 payment, that is, a

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* We need not concern ourselves with the existence or non-existence of a legal opinion (though surely there had to be one). We know that Sundstrand made a mistake.

mistaken belief that the payment was legally required (Sun App. 59-61).*

The determination of the Court of Appeals that Sundstrand purchased the Burke stock because of a mistake of law does not conflict with any valid finding of the district court. As has been seen, the district court's finding that Sundstrand acted in reliance upon defendants' representations in purchasing the Burke stock is in error and was properly disregarded by the Court of Appeals. The evidence showed what Sundstrand relied upon in entering into the January 9, 1969 agreement, and no more.

* The Court of Appeals' conviction that Sundstrand acted because of a mistake of law was reinforced by the Court's belief that Sundstrand never would have purchased the stock otherwise in view of the adverse information it had about SKI (M. App. 82-83, 84-85, 104, 105).

ARGUMENT

Each of the reasons for granting the requested writ of certiorari was urged in Sundstrand's petition for rehearing *en banc,* and rejected by the Court of Appeals. There is no need for review by this Court. The decision below is not in conflict with decisions of other courts of appeals or with any decisions of this Court. There is no important question for this Court to review. Nor is there any occasion for this Court to exercise its supervisory authority over lower federal courts.

I.

THE COURT OF APPEALS DECISION ON CAUSATION IS EMINENTLY SOUND AND IS NOT IN CONFLICT WITH ANY OTHER DECISIONS WHATEVER.

Sundstrand argues (Pet. pp. 12-17) that the Court of Appeals ignored the principles of causation applicable to actions under Rule 10b-5 because Sundstrand's purchase of the Burke stock on February 6, 1969 was in reality brought about by concurrent causes: (1) Sundstrand's reliance upon defendants' alleged misconduct, as well as (2) Sundstrand's conviction that, no matter what, it was legally obligated to complete the purchase of the Burke stock. And, the argument continues, Sundstrand's supposed reliance upon defendants' misconduct was at least *a* cause of Sundstrand's purchase of the Burke stock, and this is sufficient under the cases to establish causation for the purpose of Rule 10b-5.

There are two answers to this argument. First, Sundstrand could not have (justifiably) relied upon defen-

dants' misconduct in purchasing the Burke stock on February 6, 1969; by that time, Sundstrand had sufficient adverse information about SKI so that it had terminated the merger negotiations and its officers had divested themselves of the bulk of their SKI shares (M. App. 82-83, 84-85, 104, 105). Second, and of greater significance, the Court of Appeals held, and correctly so, that Sundstrand's mistaken conviction that it was legally bound to purchase the Burke stock was *the* cause of the purchase on February 6, 1969 (M. App. 87, 102-104, 105).

This is not a case where there were concurrent causes. On Sundstrand's own theory of this case, maintained from the beginning, Sundstrand's only reason for purchasing the Burke stock was its mistaken belief that it was obligated to make the purchase.

Contrary to Sundstrand's contention, the decision of the Court of Appeals is not in conflict with the decision of this Court in *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). *Affiliated Ute* held that, under the circumstances of that case, the withholding of a material fact in connection with the sale of a security warranted an inference of reliance or causation on the part of the seller. In the instant case, any inference of reliance or causation on the part of Sundstrand vanished in the face of the uncontroverted evidence that Sundstrand purchased the Burke stock because it believed it was legally bound to purchase it.

On the peculiar facts involved here, the decision of the Seventh Circuit on the question of causation is correct, and does not conflict with any other decision of either this Court or any court of appeals.

II.

THE DECISION OF THE COURT OF APPEALS DOES NOT CONFLICT WITH DECISIONS OF OTHER COURTS OF APPEALS INTERPRETING THIS COURT'S DECISION IN ERNST & ERNST v. HOCHFELDER, 425 U.S. 183 (1976).

Sundstrand urges (Pet. pp. 17-20) that the decision of the Court of Appeals is in conflict with various decisions of other courts of appeals interpreting *Ernst & Ernst* v. *Hochfelder,* 425 U.S. 183 (1973), primarily the decisions in *Holdsworth* v. *Strong,* 545 F.2d 687 (10th Cir. 1976) and in *Dupuy* v. *Dupuy,* 551 F.2d 1005 (5th Cir. 1977), following *Holdsworth* in principle.

Holdsworth, so far as it is of interest here, holds that if contributory fault of a plaintiff in a Rule 10b-5 case is to cancel reckless or intentional securities fraud on the part of a defendant, the fault of the plaintiff must be gross conduct somewhat comparable to that of defendant (545 F.2d at 693).

The decision below does not conflict with *Holdsworth.* Sundstrand did not fail to recover damages for its purchase of the Burke stock on account of any comparison between its conduct and that of defendants. Sundstrand failed because the evidence demonstrated that Sundstrand purchased the Burke stock on account of a mistake of law, and not because of any conduct of defendants. There was no need to compare Sundstrand's conduct with the conduct of defendants.

Moreover, the Court of Appeals was well aware of *Holdsworth.* It followed *Holdsworth* to the letter in holding that defendants were liable to Sundstrand for inducing it to enter into the stock option transfer agreement on January 9, 1969 (M. App. 81, 100-101).

There is no merit to Sundstrand's assertion that the decision below conflicts with the decision in *Holdsworth*, or with any other decision for that matter.

III.

THE COURT OF APPEALS' REVERSAL OF THE DISTRICT COURT'S DECISION ON DAMAGES IS WELL SUPPORTED BY THE TRIAL RECORD.

Lastly, Sundstrand argues (Pet. pp. 20-24) that the Court of Appeals' *crucial* determination that Sundstrand purchased the Burke stock because it believed it was obligated to do so is a finding that defendants did not seek and no party briefed on appeal, and Sundstrand says, was expressly, indeed blatantly, predicated upon material not in the trial record.

Contrary to Sundstrand's arguments, defendants have vigorously asserted, and briefed on appeal, that the only rational explanation for Sundstrand's purchase of the Burke stock was its mistaken belief that it was legally bound to make the purchase (Sun App. 59-61).

Also, it is clear from the trial record, as well as from additional material in the record on appeal (S. App. 132, 133, 139, 143), that Sundstrand mistakenly believed that it was obligated to purchase the Burke stock, and that this was the reason for the purchase.

As has been seen, it has been Sundstrand's steadfast position throughout this litigation that it was legally required to purchase the Burke stock on February 6, 1969. Its counsel so stated again and again. Sadler testified in open court that Ethington told him that Sundstrand was going to purchase the Burke stock because "our counsel

feels we are obligated to buy the stock." There can be no question but that the trial record alone supports the proposition that Sundstrand bought the stock because of a mistake of law.

So puzzled was the Court of Appeals at Sundstrand's bizarre behavior that, out of an abundance of caution, it looked under every stone. It examined certain deposition testimony that was in the record on appeal but not in the trial record. Deposition testimony of Ethington, of Sundstrand board chairman Olson, and of Schuette, make it abundantly clear that the Court of Appeals' conclusion was correct: Sundstrand bought the Burke stock because it thought it was legally obligated to do so, and for no other reason.*

Sundstrand's argument that it never needed, and therefore made no effort, to rebut or explain the material not in the trial record (Pet. p. 23) must fall on deaf ears. The material not in evidence merely corroborates the position Sundstrand took throughout the case, as well as the testimony of its president, Sadler, at the trial. Sundstrand had ample opportunity to explain or rebut the testimony of Sadler, but neither Ethington nor any other Sundstrand witness did so.

The Court of Appeals' conscientious examination of purely corroborative deposition testimony in the record on appeal is certainly no basis for this Court to exercise its supervisory power over lower federal courts.

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* Sundstrand has not seen fit to reveal the nature of the deposition testimony that is in the record on appeal but not in the trial record. Out of fairness we have included it in our Appendix (Sun App. 61-86).

IV.

THERE IS NO REASON FOR THIS COURT TO REVIEW THE DECISION BELOW.

No amount of strained argument can convert this case into one warranting review by this Court on certiorari.

The decision below turned on its own facts and, insofar as the issues raised by this Petition are concerned, affects no one but the parties to this case.

There is no conflict of decisions. There is no important question for this Court to review. There is no need for this Court to exercise its supervisory powers.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that Sundstrand's Petition for a Writ of Certiorari should be denied.

September 12, 1977.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This Brief of Respondents in Opposition has been served on Petitioner, pursuant to Rule 33(1) of this Court, by depositing three copies thereof in the United States mail box at 69 West Washington Street, Chicago, Illinois, with first class postage prepaid, addressed to W. Donald McSweeney, Esq., 7200 Sears Tower, 233 South Wacker Drive, Chicago, Illinois 60606, on this 12th day of September, 1977.

Frank F. Fowle
Counsel for Respondents

No. 77-255

In the
Supreme Court of the United States

October Term, 1977

SUNDSTRAND CORPORATION,
Petitioner,

vs.

SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., EXECUTORS OF THE ESTATE OF JOHN B. HUARISA,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

APPENDIX OF RESPONDENTS

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APPENDIX OF RESPONDENTS

I. EXCERPTS FROM SUNDSTRAND AMENDED COMPLAINT AND FROM AMENDED ANSWER OF DEFENDANTS SUN CHEMICAL CORPORATION AND JOHN B. HUARISA

Paragraph 6 of Amended Complaint

6. On or about January 9, 1969, Sundstrand and Huarisa entered into an Agreement (the "Agreement"), a copy of which is attached hereto as Exhibit I and made a part hereof, whereby Huarisa sold to Sundstrand 223,190 common shares of SKI stock, at a price equivalent to $30 per share. In payment of the purchase price, Sundstrand thereby transferred to Huarisa 5,686 shares of common stock of Sundstrand (valued at $58-7/8 per share, the closing price on the New York Stock Exchange on January 8, 1969) and agreed to pay the balance of $6,360,915.00 in accordance with a certain offer to sell, a copy of which is appended to the Agreement as Exhibit B. On or about February 6, 1969, Sundstrand, at the direction of Huarisa, paid to National Boulevard Bank of Chicago the full balance of $6,360,915.00 and took delivery of certificates for the 223,190 common shares of SKI stock.

6. Answering the allegations of paragraph 6, that on about January 6, 1969, Sundstrand and Huarisa entered into an Agreement (the "Agreement"), a copy of which is attached to the amended complaint as Exhibit I, whereby Huarisa sold to Sundstrand 223,190 common shares of SKI stock at a price equivalent to $30 per share, that in payment of the purchase price, Sundstrand thereby transferred to Huarisa, 5,686 shares of Sundstrand

common stock valued at \$58-7/8 per share, the closing price on the New York Stock Exchange on January 8, 1969, and agreed to pay the balance of \$6,360,915 in accordance with a certain offer to sell, a copy of which is appended to the Agreement as Exhibit B, and that on about February 6, 1969, Sundstrand, at the direction of Huarisa, paid to National Boulevard Bank of Chicago the full balance of \$6,360,915 and took delivery of certificates for the 223,190 common shares of SKI stock, these defendants deny the said allegations, except they admit that on January 9, 1969, Sundstrand and Huarisa entered into the Agreement attached to the amended complaint as Exhibit I, admit that the closing price of Sundstrand common stock on the New York Stock Exchange on January 8, 1969 was \$58-7/8 per share, and admit that on February 6, 1969, Sundstrand took delivery of certificates representing 223,190 shares of SKI common stock. Further answering, these defendants state that on January 9, 1969 Sundstrand promised to reimburse Huarisa for his payment (on January 8, 1969) of \$334,785, that such reimbursement was to take the form of delivery to Huarisa of 5,686 shares of Sundstrand stock valued at \$58-7/8 per share, that such shares were delivered to Huarisa on about March 3, 1969, that in consideration for Sundstrand's promise to deliver such shares Huarisa assigned to Sundstrand his right, pursuant to the offer to sell appended to the Agreement as Exhibit B, to purchase 223,190 shares of SKI stock at \$30.00 per share, that Huarisa made the aforesaid payment of \$334,785 to prevent the right to purchase those 223,190 shares from lapsing, and that,

on about February 6, 1969, approximately two weeks after the termination of acquisition negotiations, Sundstrand, voluntarily, without obligation, after a full and complete investigation of SKI, and with full knowledge of all material facts paid to National Boulevard Bank of Chicago, as agents for the sellers of such SKI shares, $6,360,915 even though the offer to sell, if accepted, called for payment of only 20% of the purchase price by February 8, 1969 and the balance by April 9, 1969.

II. ETHINGTON DIRECT TESTIMONY AS TO WHAT SUNDSTRAND RELIED UPON IN ENTERING JANUARY 9, 1969 AGREEMENT

134 Mr. Jenner: Is it offered?

The Court: It is offered and accepted.

Mr. McSweeney: It was admitted.

Mr. Jenner: If your Honor please, as to Mr. Meers we would —

The Court: You don't have to tell me that each time, I mean —

Mr. Jenner: Well, I just worry.

The Court: You want to insulate him all the way through, do you?

Mr. Jenner: Yes, sir.

The Court: I got the message to begin with.

Mr. Jenner: All right.

The Court: There is no jury.

Mr. Jenner: Yes, your Honor.

The Court: And your objection that Mr. Meers is a bystander, or whatever you want to call him later on— I will accept it for the time being.

Mr. Jenner: All right.

The Court: Until I hear some evidence.

By Mr. McSweeney:

Q. Mr. Ethington, in having Snudstrand enter this agreement of January 9, 1969, Plaintiff's Exhibit No. 4, to buy the stock, on what did you rely in making that decision?

135 Mr. Freehling: Your Honor, I object to that question.

The Court: I think that is one of the essential elements in the case. I think the witness is at least entitled to state, subject to your cross examination, as to what factors he took into consideration.

By The Witness:

A. I relied on the earnings statements that had been given to me of Standard Kollsman Company, particularly of the 86 cents a share, and also on their forecast of making $2.13 a share, and I also relied on, when I asked Mr. Meers if he thought these earnings were reasonable when we negotiated the potential merger, and he stated yes.

I also relied on the published documents of their annual report and other information that I had.

By Mr. McSweeney:

Q. Did you rely on the statements concerning the 1968 earnings?

A. Yes, I did.

Mr. Freehling: I object, your Honor.

The Court: I sustain the objection. I recognize that sooner or later, this evidence is going to get in, but do it the right way. If the witness forgets, you can take it up from there some other way.

136 Mr. McSweeney: All right.

The Court: I sustain the objection.

By Mr. McSweeney:

Q. Would you state whether there was anything else that you recall that you were relying on?

Mr. Freehling: Your Honor, I object.

The Court: Now he may answer. Overruled.

Mr. Freehling: Your Honor, this is the invidious character of a leading question. It suggests the answer to the witness so that the questioner can then say —

The Court: I suppose he is entitled to exhaust the witness' recollection, isn't he?

Mr. Freehling: He certainly is but not by asking leading questions.

The Court: As to whether he relied on anything else?

Mr. Freehling: But after telling the witness what he would like to hear, he then asks an exhausting recollection question.

The Court: Having gone through this case once, I think your gentlemen pretty well know what the answer is going to be in any event. So, I think we are sparring without results.

The objection is overruled.

137 By The Witness:

A. Yes, I relied on the earnings for 1968 of the 86 cents that were reported and the $1.16 that was forecasted, and also on the other projections that were made to me by Mr. Huarisa and also by Mr. Meers.

138 By Mr. McSweeney:

Q. Well, by other projections, did you rely on the statements as to the financial condition?

The Court: No. I will sustain the objection before it is made.

Mr. McSweeney: All right.

Mr. Freehling: Thank you.

By Mr. McSweeney:

Q. What else, if anything, did you rely on?

A. I also relied on the fact that Mr. Huarisa stated to us that the Avionics, the operation had turned around, and that the company's business was going very well.

Q. Was there anything else that you can recall?

A. Not that I can recall.

Q. Mr. Ethington, after January 9, 1969, what was your next contact, if any, with a representative of SKI, Standard Kollsman?

A. I called Mr. Meers from Rockford, Illinois, at his office at White, Weld.

Q. When was that, sir?

A. About January 20, 1969.

Q. To your knowledge, was anyone else in on the phone conversation?

A. Not to my knowledge.

Q. Would you state, sir, what was said by you and

III. SUNDSTRAND'S ADVERSE INFORMATION ABOUT SKI

(1) Meeting of November 19, 1968

Schuette Trial Testimony (1st Trial)

2858 was something that he was very familiar with as a result of having come from a TV manufacturer, and he still had some real problems with the tuner division. He said that most of his competitors had gone to Taiwan for manufacturing, and that he was having an awful time competing with them making it in the United States. He said that he was making plans to have the tuner made in Mexico, and here he felt that he could get the same advantages that his competitors were getting by having it made in Taiwan.

He said that the Casco Division was a good solid operation and a good money maker. He said that Avionics had lost money, that he had some real problems, but that he had turned it around. He said that some of the real problems in Avionics were essentially due to preproduction costs, high development costs, and overorganization.

I said to Mr. Huarisa that I sympathized with the problem of overorganization because this is generally the way in which prime contractors operate, that they force you to set up project teams to follow their particular contract, and this generally causes you then with the overorganization to have excess overhead costs associated with your particular product.

2859 So I sympathized with him very much.

With regard to preproduction costs and development, I said that anyone who is in the aviation business is quite familiar with this type of cost accumulation; that as long as we had to price on a learning curve, any one of us that are in the accessory business run into this type of cost accumulation; that in general in our operations — I stated that in our operations we looked at the amortization of pre-production costs and development costs in two ways: One, in a high-risk category and one in a low-risk category. The low-risk category was one in which you won the contract by technical evaluation because you had an engineering capability in a particular product area and you designed a product specifically for the particular end vehicle. In this particular situation your only problem really is what is the life of that end vehicle because once you have won the technical evaluation, you can certainly set up your pre-production costs and amortize them over the anticipated quantity of the production of the vehicle and it is quite safe because you won't get thrown off of the job unless you really fall

2860 flat on your face.

In the high-risk category is where you design a product to a military specification and sell it interchangeably in competition with other manufacturers who make exactly the same product. Now here price-delivery become very serious factors and the matter of amortization becomes a real high risk item.

(2) Meeting of December 3, 1968

Huarisa Deposition Testimony

103 Q. Who was present there?

A. Mr. Olson, Mr. Sadler, Mr. Ethington, Mr. Schuette and Mr. Gustafson.

Q. Would you tell us what was said at this meeting.

A. Well, I repeated what I had said at the November 19th meeting for the benefit of Sadler and Olsen and Gustafson.

Q. Will you tell us what you said at the meeting.

A. I told them the problem that I had had — the ones that were making a profit, the possibility of our tuner operation, and where we were setting up in Mexico, our new solid state tuner, and pointed out to them that — at that time they asked me again if I could deliver control of the company and I said I could, because I had first refusal with the Burke stock.

Q. What else did you say about that, anything?

A. And I think we discussed the '69 earnings again, and I think a question was brought up about '68 earnings, and I told them the same thing I told them at the Chicago Club, that I couldn't predict anything, because unless we got some orders we would be

104 faced with some write-offs.

Q. Who asked you about the '68 earnings?

A. It could have been any one of them.

Q. And what you said was you couldn't predict anything because unless you got some orders you would be faced with write-offs?

A. With some write-offs.

Q. Is there anything else you said about that?

A. Not that I can recall.

Q. Okay. What did you say about the '69 earnings?

A. The same thing I said at the Chicago Club.

Q. What was that? Will you state what you said at the meeting in the apartment on December 3rd?

A. The earnings would be between two dollars and two-fifty, but if they were going to make a proposal to use the two dollar figure, that I am sure they didn't want to dilute their earnings and we didn't want to dilute ours.

Q. What else was said?

A. I think someone made the statement that they would earn between three-twenty-five and three-seventy-five in 1969.

Q. Who said that?

105 A. I don't remember whether it was Mr. Ethington or Mr. Schuette, or one of them.

Q. Did you tell them what the write-offs would be if you didn't get some orders?

A. No, I did not.

Q. You hadn't told them that at the meeting at the Chicago Club, either, had you?

A. Yes, I had.

Q. Well, did you give them any idea as to whether the '68 performance would show the company to be in the red or in the black, or what?

A. No comment was made.

Q. No comment was made.

So, in other words, they were left to assume that it could be in the red?

A. I don't know what they could assume.

Q. Did you indicate at the meeting at the Chicago Club on November 19th, how much the write-offs would be?

A. No, I didn't.

Q. You merely told them what contracts or programs they would be related to, is that it?

A. No.

Q. No.

106 A. We did not discuss that.

Q. Oh, you didn't?

A. No, we didn't discuss the programs.

Q. Well, I want to know — going back for a moment to the meeting at the Chicago Club on November 19th, you did not discuss the programs there, either?

A. That's correct.

Q. The extent of your statement to them at the Chicago Club on November 19th was that there would be some write-offs if you didn't get some orders?

A. Roughly correct.

Q. Well, will you articulate it and make it as exactly correct as you can?

A. Well, that's about as correct as I can make it.

Schuette Deposition Testimony

161 Well, I guess I am confused. Let's start over.

Was there, in fact, Mr. Schuette, some discussion by Mr. Huarisa on December 3rd of accounting differences between himself, or Standard Kollsman and Mr. Burke?

A. The discussions related to his ability as an operating man and his ability to relate that to the accounting for profit and loss.

Q. The discussion on December 3rd related to Mr. Burke's —

A. — which was a carry over from the earlier meeting that he had indicated he had incompetent management and he had to make some changes to bring the Standard Kollsman Division into the black.

Q. What did he say about Mr. Burke's incompetency or inability to properly account for profit and loss?

A. Only that that was the statement that was made. We had no basis for questioning it.

Q. Well, to what discussion did you have reference when at Page 46 of the transcript you
162 refer to the December 3rd meeting in regard to some discussion or disagreements between Mr. Burke and Mr. Huarisa in regard to accounting procedures?

A. In talking about the write offs and how you accumulate write offs. But this was a general discussion.

Q. I understand it was a general discussion, but what was said on December 3rd about that subject?

Mr. Montgomery: If you recall.

By The Witness:

A. If I recall. I recall only a general reference to it.

By Mr. Harris:

Q. And the general reference was that there was some disagreement between Mr. Burke and Mr. Huarisa in regard to the subject of write offs?

A. Over the matter of how to manage the Division and its resultant profit and loss, of which write offs is a part.

Q. I see. But you don't exactly recollect in
163 substance what Mr. Huarisa said his disagreement was with Mr. Burke in that regard?

A. No, sir.

Q. Except that there was some?

A. No, sir, I do not.

Q. Did he tell you how that difference of opinion between he and Burke on the subject of write offs had been resolved?

A. No, sir.

Q. Did he tell you whether or not it had been resolved?

A. Only to the extent with the changes that had been made he now was bringing the Kollsman Instrument Division — no, let me correct that. Only to the extent he had now turned the Kollsman Instrument Division around.

Q. Did either of you or Mr. Ethington ask what Mr. Burke's position was in regard to the write offs?

A. No. I did not. I cannot answer for Mr. Ethington.

Q. You don't recall whether or not Mr. Ethington

(3) Meeting of December 26, 1968

Ethington Trial Testimony

108 Mr. McSweeney: I will rephrase it in that way.

By Mr. McSweeney:

Q. What then with respect to this transaction in your view was the significance of earnings per share?

A. The significance of earnings per share in my view at that time was in adding the two companies together, you would add their total profits, and then the total number of shares that you would issue in the merger and see what your earnings per share would come out so that there would be no dilution in the surviving company's earnings. So, that would become very important in merging two companies together.

Q. Now, carrying on, sir, after the December 3, 1968 date, when was the next meeting or contact with either Mr. Huarisa or Mr. Meers?

A. The next meeting was on December 26th in the morning.

Q. Where did that meeting take place?

A. That took place in Rockford, Illinois, in Mr. Sadler's office.

Q. Would you please identify Mr. Sadler? I don't know that we have done that.

A. Mr. Sadler was the executive vice president of Sundstrand at that time. He is president now.

Q. Now, at this meeting on December 26th, who

109 was present?

A. Mr. Sadler, Mr. Huarisa, Mr. Schuette and myself part of the time.

Q. Can you state on this occasion, what did Mr. Huarisa say in this conversation?

A. Mr. Huarisa stated that he had brought with him new projections for Standard Kollsman for the year 1969. The new projections for the year 1969, he stated, would be $2.13 per share rather than the $2.41 per share.

However, he stated in his opinion that he still felt that the company would probably earn at least $2.50.

Mr. Huarisa also stated that the 1968 earnings as reported were 86 cents a share, and that if there would be any adjustments, that in no case would there be any adjustments that would affect what had already been reported.

The Court: 86 cents a share for what period?

The witness: For nine months in 1968.

By Mr. McSweeney:

Q. Go ahead.

A. Mr. Huarisa then gave me a copy of the new projections. I stated that we had worked out a preliminary proposal for Sundstrand to merge Standard Kollsman into Sundstrand, and that it amounted to approximately $32.25 per share. Mr. Huarisa stated that he did not believe that this was high—

(4) Ethington personally directs Sundstrand's survey team to investigate and report on SKI's deferred costs

Ethington Trial Testimony

361 By Mr. Fowle:

Q. Mr. Ethington, you knew in early January 1969 that SKI was carrying deferred pre-production costs on its books as an asset, didn't you?

A. Yes, I did.

Q. You learned this in December 1968, I believe, isn't that true?

A. Yes, I did.

Q. Now, you recall that one of the things that the finance group of the investigative team was instructed to do was to obtain an explanation and list of these deferred pre-production costs, don't you?

A. Yes, I do.

Q. Wasn't it you, yourself, Mr. Ethington, who gave that particular instruction?

A. Yes.

Q. To the finance team?

A. Yes, it was.

Q. You recall, don't you, that the survey of SKI began on January 7th or thereabouts?

A. That is correct.

Q. This was a Tuesday, if you will remember?

A. I don't know.

Q. Well, January 6th, the day that you were in the office—

(5) By January 10, 1969 Sundstrand regards SKI deferred cost and other problems as serious

Sadler Trial Testimony

470 A. That is right, 600 shares.

The Court: He already answered the question and so that solves your problem, it would seem to me. Go ahead.

By Mr. Freehling:

Q. Thereafter, on December 26, you had the meeting with Mr. Huarisa at Rockford that you have described, is that right?

A. That is right.

Q. And on December 30, you went out and purchased another 1,000 shares of Standard Kollsman stock for your own account, isn't that right?

A. That is right.

Q. I show you what has been marked as Defendant Sun-Huarisa Trial Exhibit 36-G—after first showing it to your counsel—and ask you, sir, if that's your confirmation of your purchase of 1,000 shares of Standard Kollsman stock on December 30, 1968?

(Tendering document to witness.)

A. (Witness examining) Yes, that is right.

Q. Now, Mr. Sadler, you told us about your visit to Kollsman Instrument Corporation on January 10, 1969; do you recall that?

A. Yes, I do.

471 Q. Before you went into the meeting that you have previously described with Mr. Katz and Mr. Allwarden and various others, there was a meeting of the Sundstrand group, was there not?

A. You mean the team people?

Q. Yes, the Sundstrand investigation and examination team?

A. Yes. There was one or more meetings; I don't know specifically which one you are referring to but there were preparatory meetings, yes, if that is what you have in mind.

Q. Well, there was a meeting, was there not, on the morning of January 10, 1969—

A. Oh, yes. I see.

Q. Attended by you to bring you up to date with what the team had discovered up to that point?

A. You mean this was an exclusive meeting with Sundstrand people before meeting with them?

Q. Sundstrand only—

A. Yes.

Q. —and no Standard Kollsman or Kollsman Instrument?

A. Yes, yes, absolutely.

472 Q. And at this meeting—let's call it a private meeting or Sunstrand meeting, Mr. Rothstein, whom you have already told us about, provided the rather disquieting information about the office union, isn't that right?

A. Well, that was one small portion of it, yes.

Q. But you told Mr. Rothstein that that was nothing new, you had learned about that in December when you were East with Mr. Huarisa, isn't that right?

A. Well, that particular thing, yes.

I said that it hadn't spread to Casco yet, as I believe it went, and that I had known about that particular item, yes, but not about the committeeman or many of the other practices, no one had told me about those.

Q. And at this private Sunstrand meeting Mr. Ross and Mr. Landstrom and Mr. Cascio, the financial group, gave a report or told you what they had been doing, isn't that right?

A. That's right.

Q. And they pointed out financial problems, did they not?

A. Yes.

Q. They told you about outstanding contracts on which the completion costs appeared troublesome?

A. Yes.

Q. And they told you about deferred preproduc-
473 tion costs, isn't that right?

A. Yes.

Q. And there were a number of other people who also reported at that Sunstrand meeting, isn't that right?

A. That is right, on the various other problems I have mentioned.

Q. And when you got done hearing all of these reports at the private Sunstrand meeting the morning

of January 10, you said that these things sounded pretty serious, didn't you?

A. I certainly did, yes.

Q. And you said that you should listen to the Kollsman Instrument people to see if there were any reasons for going ahead, isn't that right?

A. That is right.

Q. And then you went into the meeting with the Kollsman Instrument personnel that you have previously described?

A. That is right.

Q. And in the course of that meeting with the Kollsman Instrument personnel, some of the Sunstrand team members asked questions, did they not?

A. They did, yes.

Q. For example, they asked how there was going to be recovery of these preproduction costs, isn't that right?

A. Yes.

474 Q. And they asked why it was logical to defer these costs?

A. Yes.

Q. And there was discussion about cost overruns, was there not?

A. Potential cost overruns, yes.

Q. And claims against the Government?

A. Yes.

Q. And startup costs?

A. Yes.

Q. And there was considerable discussion about how substantial preproduction costs had been built up in connection with anticipated business, is that right?

A. Well, when you say "discussion," we asked questions and they told us how they felt they would circum-

vent the problems so there would be no degradation of earnings, so, yes,—

Q. All right.

A. So, they answered our questions. Yes.

Q. And they also told you what would happen if the orders were not received, isn't that right?

A. Well, I must say you are taxing my memory in terms of the degree of this. I am sure that there must have been some statements along that line but I, I can't, you know, at this moment tell you exactly what was said.

(6) By January 13, 1969 Sadler advises Ethington he is very pessimistic about SKI

Sadler Trial Testimony

475 Q. There was optimism expressed that the orders would come in, is that right?

A. There was optimism expressed by the Standard Kollsman people, yes, that they would get them.

Q. Then, Mr. Sadler, at the conclusion of that long day at Elmhurst, New York, on January 10, you and some of the team members flew home together in the Sundstrand plane, is that right?

A. That is true.

Q. There was you and Mr. Reif, Mr. Hucker, Mr. Rothstein and Mr. Erikson, isn't that right?

A. As best I remember, that sounds right. Yes, probably so.

Q. Of course, during that plane ride home, you had discussion about what you had seen and heard, isn't that right?

A. I am sure we spent some time on it. I would guess we would have.

Q. The five of you discussed doubts concerning future problems that would be faced if the companies merged, isn't that right?

A. I would say we probably did.

Q. And expressed concern about contract problems, lack of product synergism, and concluded that the answers that you had received had not been adequate to satisfy your doubts, isn't that right?

A. Well, it seems to me that your words are very
476 close. I would say that our feeling at that point—we hadn't heard from the Midwest team in terms of what was going to happen there. We certainly had reached no final conclusion but we were discouraged because of the reasons that I gave here in my direct testimony. So, there was a feeling of pessimism at that point, I agree.

Q. Upon your return to Rockford, you gave a report to Mr. Ethington, Mr. Schuette and Mr. Olson about what you had seen and heard, is that not right?

A. Would you include the word "preliminary" because in no sense was it meant to be a final conclusion.

Q. No, but it was a preliminary report?

A. Sure.

Q. A report of what you had seen so far?

A. We had adjacent offices. It was logical I told him what was going on.

Q. Do you recall that January 10, 1969, was a Friday?

A. Yes. Yes, it was a Friday.

Q. You gave your report to Messrs. Ethington, Schuette and Olson the following Monday, January 13, isn't that right?

A. I couldn't at this moment tell you whether it was then or that Saturday or the next Tuesday. It depended on when someone was available.

There was no formal meeting if that is what you have in mind.

Q. Mr. Sadler, isn't it a fact that that report 477 was made on January 13, 1969?

A. Well, as I said, there was no formal meeting. I am sure that I talked to any and all of those people that were there and available at that time because they were all interested, but I am not conscious of any meeting where we all sat down in a formal sense. I would say basically the answer is yes but I just want to differentiate: no formal meeting as such.

Q. Whatever form the meeting took, it took place on Monday, January 13, 1969?

A. There was no formal meeting.

There was a formal meeting on January 20th.

The Court: Well, the discussions took place on the following Monday after your Friday return?

The Witness: Very good. That I buy exactly.

The Court: All right.

By Mr. Freehling:

Q. At that discussion, you told Messrs. Ethington, Schuette and Olson that you had doubts about the labor situation and you were disappointed concerning synergism and you were disappointed concerning future earnings of the company, isn't that right?

A. I would presume that is so, yes.

Q. And you recall that that is what happened, don't you?

A. It is a long time ago. I think that is what happened.

(7) On January 20, 1969 Sundstrand concluded that SKI was carrying on its books over $4,000,000 of uncovered preproduction costs

Ross Trial Testimony

619 Q. I am sorry. I am back now to the meeting on January 20 in the morning with the Sundstrand team.

You discussed deferred preproduction costs, did you not?

A. Yes.

Q. You told the team members how much was deferred, how much was written off and how much remained, isn't that right?

A. Yes.

Q. What did you say?

A. I don't recall the specific words nor the specific amounts but it is outlined in the document itself.

From what I said, I told them about the amounts they had on their books, the amounts they had amortized, what the estimated costs of completion were.

I told them about the program of KIC or Standard Kollsman to evaluate the programs on a quarterly basis; that at any time they felt there was an overrun, to write those off.

I am sure I told them about the fact that Mr. Werle had indicated they had written off $600,000 in November 1968 or that month would have been profitable.

I am also sure I told them about the $902,000 question where Mr. Ryan and Mr. Werle had stated that as a
result of their program of amortizing the prepro-
620 duction costs starting with the first date of delivery,
that under that program, they would amortize $900,000 in 1968, but that as a result of the conversations with

their auditors, they would actually write off less than that.

Also, I am sure I told them that the Standard Kollsman personnel had continually assured us that they were going to get sufficient business to cover these preproduction costs.

Q. When you got all done—Were you through?

A. Yes.

Q. When you got all done stating that, you told the team that the company had $4,700,000 of deferred preproduction costs on its books, isn't that right?

A. Would you give me that question again, please.

Q. I said when you got all through telling the team members what you just mentioned, you told the team that Standard Kollsman had incurred $4,700,000 of deferred preproduction costs, isn't that right?

A. Yes.

Q. You told the team that only $600,000 of that $4,700,000 was covered by orders on the books, isn't that true?

A. Yes.

Q. You told the team that the remaining $4,100,000
621 of deferred preproduction costs would have to be
expensed at some point in the future, isn't that right?

A. I don't recall the conversation but I am sure that I told them that that would need to be amortized over the three-year period.

Q. You told the team that Standard Kollsman had not yet covered this $4,100,000 of deferred preproduction costs, although company personnel said they would get future orders to cover these costs, isn't that right?

A. Yes.

Q. You told the team that the question remained as to whether they will or whether they won't get those future orders, isn't that right?

A. No.

Mr. Freehling: Your Honor, I am going to need just a moment, your Honor.

The Court: All right.

(Brief pause.)

By Mr. Freehling:

Q. Mr. Ross, your deposition was taken over the course of a number of days. Do you recall that?

A. Yes.

622 Q. On page 980 were you asked these questions and did you give these answers:

"Q. In your report wherein you indicated"—

In Meers' Exhibit 9, that was a deposition exhibit—". . . that of that 4.7 million development projects to be amortized, $600,000 is covered by orders on the books. Did that relationship between orders on the books and deferred costs raise a question in your mind as to the ability of Standard Kollsman to amortize those costs?

"A. Yes, that's what we spent several hours asking Standard Kollsman questions about the previous two weeks.

"Q. And did you express your concern on that subject in the first meeting on January 20th?

"A. Yes, I am sure we said 'They have not yet gotten them covered and they said they are going to get future orders.' It is a question of whether they will get future orders."

Did you give those answers to those questions?

A. I don't recall it, but that probably—I think that that is probably there.

Q. Did you make those statements at the team meeting on January 20, 1969?

A. I do not recall the specific words. I am sure I
623 indicated the amount that was covered and the amount that they had to get covered, or would have to amortize.

Q. And you also said that you had serious doubts about whether they would ever get the contracts to cover the balance, isn't that right?

A. I don't recall that.

Q. And there was discussion at this meeting of the team on the morning of January 20, 1969, about Standard Kollsman's calculated 1968 earnings per share for the first 11 months of the year, do you recall that?

A. I'm sorry, may I have that again, please.

(Question read by the reporter.)

By The Witness:

A. We knew what the 11 month's earnings were.

By Mr. Freehling:

Q. You knew that they were 84 cents per share?

A. Yes.

Q. And you knew that that was a decline from the reported 86 cents per share for the first 9 months of the year, is that right?

A. Yes.

Q. Now, Mr. Ross, following this team meeting on the morning of January 20, there was a meeting held with Mr. Ethington, is that correct?

A. That I attended?

Schuette Deposition Testimony

124 Q. Do you recall any other attempts to obtain information during December or January from a source other than Standard Kollsman?

A. No, sir.

Q. Now, there were several meetings held at Sundstrand on January 20th?

A. Right.

Q. Concerning the evaluation that Sundstrand had made of Standard Kollsman, is that correct?

A. That is right.

Q. Did you attend either or both of those meetings?

A. I did not attend the meeting of the team.

Q. The first meeting was a meeting attended by the men who were on the investigating teams?

A. Yes.

Q. And you did not attend that?

A. I did not attend that.

Q. Then was there a second meeting?

A. Yes, sir.

Q. Who attended the second meeting?

125 A. Mr. Sadler, Mr. Miller, Jim Ethington, and myself.

Q. Mr. Ethington had not attended the first meeting?

A. To the best of my knowledge, he did not.

Q. How about Mr. Sadler and Mr. Miller; had they attended the first meeting?

A. I know Mr. Sadler did.

Q. You don't know whether or not Mr. Miller did?

A. It is a reasonable assumption. He was a part of the team at that time. I do not know specifically.

Q. Relate for me as best you can the substance of the conversations the four of you had at the second meeting on January 20th.

A. That, in general, we should call off the merger, or any further attempts to proceed with the merger, I should say.

Generally, there were three basic problems. One was that we would not obtain the compatibility of products or the systems concept that we had envisioned.

126 The second was the potential difficult labor problems.

And the third was the overestimation of the earnings.

Q. Now, were these three things reasons given by one of the four of you for a conclusion that the merger negotiations should be concluded or broken off?

A. I did not get your question.

Q. You just told me about three reasons—

A. Yes.

Q. —leading to the conclusion that merger negotiations should be terminated.

A. Right.

Q. Did one of the four of you list these three reasons at the meeting, or was there a general discussion?

A. There was a general discussion of them.

Q. Who was it that talked about the existence of labor problems?

A. Mr. Sadler discussed it as a result of a
127 memorandum that had been prepared by our vice president in charge of personnel.

Q. What did he say specifically about that problem?

A. I don't remember specifically.

Q. Was there some discussion of a problem of lack of compatibility, do you say?

A. Yes, sir.

Q. Who was it that discussed that problem?

A. That was discussed between Mr. Sadler and I.

Q. What specifically was said on that subject?

A. That the product which they had did not have the technical content and did not have the product mix which would give us the systems capabilities that we desired.

Q. All right. Do you recall anything else specifically said on that subject?

A. In that meeting?

Q. Yes, sir.

A. No, sir.

Q. And someone discussed the overestimated earn-
128 ings?

A. Yes, sir.

Q. For Standard Kollsman?

A. Yes, sir.

Q. Who discussed that?

A. Mr. Miller and Mr. Ethington.

Q. What did they say on that subject?

A. We got into the discussion of the deferments, the method of write-off and the probability of coming up with the earnings which had been projected.

Q. And after discussing the deferral and the matter of write-off, it was concluded that the probability of coming up with the projected earnings was not good?

Mr. McSweeney: I object to the question: Was it concluded. It is asking him for a conclusion which may have been something in his mind. The question should should be confined to what was said.

Mr. Harris: Read the question.

129 (Question read by the reporter.)

By Mr. Harris:

Q. Is that correct, Mr. Schuette?

A. I refuse to answer.

Mr. McSweeney: You may answer the question if you can. I will tell you if I want you to decline to answer. I am objecting to the question because of certain technical objections which I have stated.

The Witness: I see. Will you read the question again.

(Question read by the reporter.)

Mr. McSweeney: I did not mean to jounce it out of your mind.

By The Witness:

A. Yes.

By Mr. Harris:

Q. Did either Mr. Miller or Mr. Ethington say that it was their judgment that Standard Kollsman could not meet its projected earnings as a result of these two matters that you have referred to; that is, the defer-
130 ment and the method of write-off?

Mr. McSweeney: I am not going to object.

By The Witness:

A. Yes.

By Mr. Harris:

Q. Do you remember which one of them said that, or did they both say it?

A. It was a joint conversation.

Q. Do you recall anything specifically that they said about the deferments or about the method of write-off?

A. Nothing specifically.

Q. When you were talking about deferments, you were talking about pre-production costs which were deferred and carried on the books as assets, is that your understanding?

A. Well, I would have to answer that no, because it is much more encompassing than what you have asked.

Q. Okay. What was encompassing?

131 A. Well, it is just more than pre-production costs.
It is deferment of an accumulation of expenses that generally accompany any new product which you bring out in the aviation field. When you are working on a learning curve, it all depends how you defer it. Whether it is pre-production. There are a number of deferrals of different types.

Q. In any event, they are considered for or deferred, and the balance sheet effect of that is that they are carried as assets.

Mr. McSweeney: Now I object to that. Let me finish my objection. It is ambiguous whether you are talking or asking about what was said in conversation or some theory he has on deferral and pre-production costs.

Mr. Harris: I am talking about what was said in the meeting.

(Question read by reporter.)

Mr. McSweeney: He wants to know what was said at the meeting.

Mr. Harris: I will strike the question.

132 By Mr. Harris:

Q. The discussion that occurred at the meeting on the subject of deferrals was a discussion of deferred costs which showed up on the Standard Kolisman balance sheet as assets, is that correct?

A. I don't know. I am not an accountant.

Q. You don't know what the balance sheet effect was of the deferrals that were being discussed by Mr. Miller and Mr. Ethington?

A. Not specifically. Not specifically.

Q. Did either Mr. Miller or Mr. Ethington state an opinion as to what a more realistic projection of Standard Kollsman's earnings would be for the year 1969?

A. Yes.

Q. And what did they state in that regard?

A. I don't remember.

Q. Something under \$2.00, I take it?

A. Something under \$2.00.

Q. Do you remember whether it was under \$1.00?

A. I don't remember.

Sadler Trial Testimony

449 There was also the matter of the tuner that we had checked out. I had some people that I knew in

the industry and got a very good recommendation on the quality and acceptability of the Standard Kollsman tuner. This is a television tuner that they made and was a significant product item with them. But in investigating their facilities for manufacturing tuners, the work conditions in their Wisconsin operation were not good.

Mr. Huarisa told me that the solution to this problem was to set up a value-added plant along the border of Mexico. The competition had gone to Asia to build their tuners because of low labor. He said that we could do it through the Mexican thing.

Well, when we looked at the Mexican facility, it was nothing but a storefront, really—I will say an idea. I think it could have been developed all right, but it wasn't at that time. There would have been close-down costs in the Wisconsin plant to do it. There was a longer range question, about two or three years ahead, as to whether the value-added treatment was going to be continued to be allowed. So, this was a matter of concern to us that we felt made the merger not as attractive as we might otherwise had hoped that it would be.

Finally, there was some degree of question on the matter of earnings. We had probed this very deeply as best we possibly could with our team. We had several financial people involved in the thing because we
450 knew they were having some problems on pre-production costs and on cost overruns and some contract claims with the government and such. So, we tried to find out what we could. They gave us their rationales about what they were going to do to cover the situation and keep their earnings up and so on. Some of it we understood, and I think felt could be accomplished, but in aggregates it seemed to us they were slightly optimistic in their earnings projection both for 1968 and 1969.

Our team concluded—as you can well imagine, this is a terrible judgment thing because there was no way in three or four days that we could possibly get and digest enough information on the financial end—and we had no access to records except as they themselves provided them—to evaluate just how effective they would be in these things. So, our various team members had different thoughts about what type of earnings degragation there might be, but there was a general feeling that there would be some.

On the 1968 earnings, the team estimates on production and earnings were instead of $1.16, they might be anywhere from a dollar to 80 cents.

In the case of the 1969 earnings, again, there was quite a spread, different people thinking different numbers. The most pessimistic of these was in the $1.45 to $1.50 range and other numbers above that.

Ethington Trial Testimony

362 A. Yes.

Q. The survey lasted until what, about January 16th, was it?

A. I believe it lasted until around the 16th of January.

Q. Now, do you recall that Mr. Sadler and Mr. Erikson went to New York and met with the investigating team on the morning of January 10th?

A. I know they went to New York but I don't remember what day.

Q. But they went to New York to meet with the full investigating team, did they not?

A. Not the full team. Just those that were in New York.

Q. Do you recall that Mr. Sadler came back to Rockford after he had had this meeting with the team on January 10th?

A. No, I don't recall the date.

Q. Well, you recall that he came right back after being there a short time?

A. Yes, but I don't recall it was January 10th.

Q. I see. Now, he gave you a report, of course, didn't he, as to what the investigating team told him at this meeting?

A. I can't recall that.

Q. You mean Mr. Sadler didn't give you any kind of report as to what he learned from the investigating team or a portion of it in New York during that week?

363 A. I don't recall that he gave me a separate report just on the New York findings.

Q. Well, did he give you and Mr. Schuette a report?

A. Yes, he did.

Q. The two of you?

A. Yes.

Q. He reported to both of you?

A. Oh, yes.

Q. Isn't it true that Mr. Sadler stated to you when he got back from this visit to New York with your investigating team down there that he had developed some doubts as to whether Sundstrand should pursue the SKI investigation?

A. I don't know whether it was after that trip that but he did say that to us, yes.

364 Q. Well, at about what time did he say this to you?

A. Some time in the middle of January.

Q. Didn't Mr. Miller advise you when he returned from New York — he was part of the team that was down in New York that week of January 7th, wasn't he?

A. I don't remember if Mr. Miller went to New York or to Elmhurst. I would have to check which one he went to.

Q. Didn't Mr. Miller tell you when he got back from New York —

A. I don't think he was in New York, sir.

Q. I may be wrong about that, Mr. Ethington.

A. I think you are.

Q. My co-counsel says that Mr. Miller didn't go to New York. So, let's forget that.

Hadn't you, yourself, in the middle of January begun to develop some questions about the wisdom of this acquisition of SKI?

A. In the middle of January, I did.

Q. I mean, on January 14, 1969, you placed an order with your broker to sell the 2,000 shares of Standard Kollsman stock that you had bought on December 27th, didn't you?

A. That is correct.

Q. Mrs. Ethington sold the few shares that she had on January 17th, didn't she?

365 A. I think that I sold those.

Q. Do you know whether Mr. Sadler owned any stock, SKI stock, in the middle of January?

A. I think in the middle of January, I knew that he did.

Q. I mean, do you know that he sold 1,000 shares of SKI stock on January 17th?

A. No, I do not, or did not.

Q. I hand you, Mr. Ethington, two documents marked Defendant Sun-Huarisa Trial Exhibit 20-A and 20-B for identification, purporting to be confirmations from Bear, Stearns & Company of sales on the account of you and Mrs. Ethington of SKI stock on January 14, 1969.

I ask you if you can identify them for me?

A. Yes, I can.

Q. Will you tell me what they are, please?

Are they what they purport to be?

A. Yes, they are.

Q. The whole survey team, the whole SKI survey team had a meeting on the morning of January 20, 1969, is that right?

A. I believe that is correct, sir.

Q. Were all of the members there so far as you know?

A. I do not know. I was not at the meeting.

366 Q. This meeting lasted most of the morning, didn't it?

A. I do not know how long it lasted. Mr. Sadler ran the meeting.

Q. Was Mr. Schuette at the meeting?

A. No, he was not.

Q. Mr. Ethington, let me show you three documents which I have had marked as Defendant Sun-Huarisa Trial Exhibit 21-A, 21-B, and 21-C for identification, purporting to be copies of an agenda for what I believe to be the team meeting on January 20 at 9:30 a.m.

I ask you if you can identify those for me?

A. I can read that they are the Standard Kollsman agenda.

Q. Well, aren't these three documents —

The Court: I assume counsel will agree that if you have got the documents, they are what they purport to be?

Mr. McSweeney: We don't have them here in the courtroom but we can check them and come back to them.

By Mr. Fowle:

Q. It is true, Mr. Ethington, isn't it, that one of these is a pencilled copy of the agenda for the meeting that morning and the other two are typewritten copies of the same agenda?

A. Well, I would have to read everything to see
367 if they are the same. One is written in longhand and two are typed. I don't know if they are identical or not.

Mr. Fowle: Don't we have a stipulation covering this?

The Court: Well, you aren't going to get any help from the witness. So, if you have a stipulation, that will take care of it.

The Witness: I would have to proofread it all.

The Court: We don't want to spend that time.

Mr. Fowle: Excuse me just a moment, Judge.

The Court: I will excuse you longer than that. We will take the morning recess. I will be back at 20 minutes to 12 sharp.

Mr. Fowle: Thank you.

(Whereupon, a brief recess was taken, after which the following further proceedings were had herein:)

Mr. Fowle: With the Court's permission, I would like to refer the witness again to the exhibits, Defendant Sun-Huarisa Trial Exhibits 21-A and 21-B for identification.

By Mr. Fowle:

Q. You know what these documents are, don't you, Mr. Ethington?

A. By reading them, I can see what they are, yes.

368 Q. Well, one of them was marked Exhibit DX8 and the other DX9 during the taking of a deposition. Do you recall that?

A. No, I do not recall that.

Q. But you know what these documents are?

A. Yes.

Q. They are the agenda for the January 20 meeting, are they not?

A. That is what it says, yes.

Q. Well, but that is the fact, isn't it?

A. I was not at the meeting. I don't know if the agenda was used or not.

Q. Well, this was prepared as the agenda for that meeting?

A. That is correct.

Q. There came a time in January 1969, did there not, when you learned or you were advised that as of November 30, 1968, SKI was carrying on its books as an asset approximately $4,700,000 in deferred preproduction costs, is that true?

A. Could I have that question reread, please. I didn't hear the dates.

Mr. Fowle: Would you read it back, please.

(Question read.)

369 By The Witness:

A. Yes, I believe that is.

By Mr. Fowle:

Q. Now, you were told this on January 17th or January 20th, 1969, by either Donald Miller or Mr. Ted Ross, weren't you?

A. Yes, I was.

Q. Now, you did not attend, as I think you testified, the meeting of the investigation team on January 20?

A. I did not.

Q. As I understand it, there was a smaller meeting held after the team meeting in your office, am I right?

A. That is correct.

Q. We have referred to that sometimes in the past as the little meeting, have we?

A. I don't know, but that is what it was.

Q. Who attended this smaller meeting?

A. Mr. Schuette and Mr. Sadler and myself. I am not sure if Don Miller was there or not.

Q. How about Mr. Ross?

A. He might have been, too, but I am not sure if he was there or not.

Q. Well, at this smaller meeting, Mr. Sadler reviewed for you and Mr. Schuette what had taken place at the team meeting, is that correct?

* * *

373 Q. Was there any discussion of the so-called SKI-M125 claim against the United States Government?

A. Yes, I think there was.

Q. And what was that discussion?

A. I can't recall, I think it involved some lawyer by the name of Joy, but I don't remember the details.

Q. Well, now, didn't Mr. Sadler indicate to you that the team members were doubtful as to whether this claim would ever be paid by the United States Government?

A. Yes, that is true, that was their opinion.

Q. Now, was there — would you say that again?

A. That was their opinion.

Q. Well, now, there was discussion at this smaller meeting in your office of the 4.7 million of deferred production costs that SKI was carrying on its books, wasn't there?

A. Yes, there was.

374 Q. And it was mentioned at this meeting, was it not, that of the 4.7 million preproduction costs, only about $600,000 worth were covered by orders on the books?

A. In their opinion, yes.

Q. And it was reported to you at this smaller meeting, was it not, that the survey team did not see how it would be possible for SKI to amortize these costs because they could see no production units to amortize them on, isn't that true?

A. That is correct.

Q. Now, at this time, at the time of this meeting, you were familiar with the various SKI programs in which production costs, preproduction costs, had been deferred, were you not?

A. I knew some of them, yes. I wasn't familiar but I knew some of them.

Q. You knew something about the CPU-46?

A. I knew about some of those, yes.

Q. And the AAU-19?

A. Yes.

Q. And the KS-200?

A. That doesn't ring a bell. That does not ring a bell with me right now but I knew some of the programs.

Q. Then you and Mr. Schuette and Mr. Sadler and
Mr. Miller, if he was there, discussed the likelihood
375 of SKI being able to amortize these expenses against
the various programs and concluded that it was not
going to be feasible, isn't that true?

A. In our opinion we did not know how they could do it.

Q. Well, in your opinion, yes, you concluded that it was not feasible, in your opinion?

A. Yes.

Q. Then you and Mr. Schuette had a still further meeting in your office, I believe, is that true?

A. That is correct.

Q. You met for an hour or so after this intervening meeting?

A. Yes, approximately.

Q. And there was further discussion at this meeting, was there not, about the 4.7 million of SKI deferred preproduction costs, was there not?

A. Yes, there were.

Q. I didn't hear your answer.

A. Yes, there was.

Q. By this time, Mr. Ethington, you certainly had no confidence in any of the representations that had been made to you, as you say, that SKI's 1969 earnings would be $2.13 or $2.41, did you?

A. I lacked confidence, yes.

376 Q. You had no confidence in those figures at all by January 20, isn't that right?

A. Not at that date.

Q. By that date you had no confidence?

A. That is right.

Q. In fact, someone on the investigating team had estimated that SKI's 1969 earnings would not exceed $1.45 a share, isn't that true?

A. That is true.

Q. Now, you and Mr. Schuette and Mr. Meers and Mr. Huarisa had a meeting at the O'Hare Inn, is that correct, that same day?

A. That evening.

Q. January 20?

A. That evening, yes.

Q. It was a long meeting, was it not?

A. Several hours.

Q. And the purpose of this meeting was for the representatives of Sundstrand to tell the representatives of SKI that the negotiations would be terminated?

A. That is correct.

Q. Is that correct?

A. That is correct.

(8) Ethington and Schuette meet with Huarisa and Meers on January 20, 1969 to terminate merger negotiations with SKI and to explain the reasons

Schuette Deposition Testimony

134 Q. Was someone specifically delegated that task?

A. Mr. Ethington was going to make these arrangements.

Q. Do you know, in fact, what Mr. Ethington did in that connection?

A. No, sir.

Q. Did Mr. Ethington get in contact with Mr. Meers either on the 20th or shortly thereafter?

A. There was a meeting established out at the O'Hare Inn, and that is all I know about it.

Q. When was that meeting held?

A. January 23rd. The evening of January 23rd. To the best of my recollection, it was in the evening meeting.

Q. Excuse me. What was that last?

A. It was in the evening meeting.

Q. Were there two meetings on the subject of Sundstrand withdrawing from the Standard Kollsman proposal?

A. Yes, sir.

Q. The first one was on January 23rd, to your
135 recollection?

A. As I recall it.

Q. And when was the second one?

A. Two days later.

Q. The first one was at Sheraton-O'Hare?

A. Right.

Q. The second one, where was it?

A. At the Chicago Club.

Q. Who attended the first meeting at the Sheraton-O'Hare?

A. Mr. Huarisa, Mr. Meers, Mr. Ethington, and myself.

Q. How long a meeting was that?

A. Three-and-a-half hours. Only because Mr. Meers was late getting there.

Q. I see. How late was Mr. Meers?

A. Forty-five minutes, I would say.

Q. If you can, relate for me the substance of the conversation between you, Mr. Huarisa and Mr. Ethington prior to the time that Mr. Meers arrived?

A. It was just a general conversation.

136 Q. You don't remember anything specific?

A. Not with relation to the subject matter, no.

Q. All right. Relate for me the substance of the conversation as you recall it, after Mr. Meers arrived?

A. We outlined to Mr. Meers and Mr. Huarisa the three points to which I have already testified. My part of it was to go into much more detail with regard to the compatibility. Following the January 21st meeting, I had a meeting with our Mr. Robinson who was a part of this team to get very specific, with regard to what we expect. What did they have, and how compatible were they.

Q. Is that the Mr. Robinson who was at United Control?

A. Yes, sir.

Q. So following the meeting that the four of you had on the 20th, you met with Mr. Robinson on the subject of compatibility or lack of compatibility?

A. That is right.

137 Q. Between Sundstrand and Standard Kollsman?

A. That is right.

Q. Then at the meeting at the Sheraton-O'Hare, Mr. Ethington also listed the three reasons for Sundstrand's disinterest?

A. That is right.

Q. And you discussed in details the —

A. The lack of compatibility.

Q. All right. What else was said at the meeting at the Sheraton-O'Hare?

A. We were discussing in general the labor situation.

Q. Who did that?

A. I would say jointly, Mr. Ethington.

Q. You and Mr. Ethington?

A. Right.

Q. That was a problem of increased labor rates that Sundstrand would face if it acquired Standard Kollsman?

A. Together with the presence of an office union and its possible spreading to our other operations.

138 Q. All right. And what else was said at the Sheraton-O'Hare meeting?

A. There was a discussion by Jim with regard to these deferred items and he went into detail with respect to them.

Q. What do you recall of that detailed discussion?

A. That the general conclusion was that we did not think that they were going to be able to earn the money which had been forecast.

Q. As a result of the deferred items?

Mr. McSweeney: Well, what is the question?

(Question read by the reporter.)

Mr. McSweeney: I object to the question. Are you asking what was said?

Mr. Harris: Yes.

Mr. McSweeney: All right. What was said, he is asking.

By The Witness:

A. Mr. Ethington discussed the deferred items
139 as well as the number of other accounting problems that he foresaw. I guess, problems is the word.

Q. What specifically were those problems that he said he foresaw?

A. I don't remember them.

Q. You don't remember anything other than the deferred items?

A. I don't remember, really, the detailed discussions because of —

Q. Do you remember any of the specifics that he said in relation to the deferred items?

A. I don't recall them in detail.

Q. Do you recall anything else that anyone said at the Sheraton-O'Hare meeting?

A. In chronology, I guess the next thing that was discussed was the disagreement with our analysis with — by Mr. Huarisa. And that generally he would like to convince us that these items were a lot less risk items than we felt that they were.

Q. Did Mr. Huarisa say that he disagreed with all three points of your analysis?

A. No.

Ethington Trial Testimony

376 Q. You had no confidence in those figures at all by January 20, isn't that right?

A. Not at that date.

Q. By that date you had no confidence?

A. That is right.

Q. In fact, someone on the investigating team had estimated that SKI's 1969 earnings would not exceed $1.45 a share, isn't that true?

A. That is true.

Q. Now, you and Mr. Schuette and Mr. Meers and Mr. Huarisa had a meeting at the O'Hare Inn, is that correct, that same day?

A. That evening.

Q. January 20?

A. That evening, yes.

Q. It was a long meeting, was it not?

A. Several hours.

Q. And the purpose of this meeting was for the representatives of Sundstrand to tell the representatives of SKI that the negotiations would be terminated?

A. That is correct.

Q. Is that correct?

A. That is correct.

377 Q. Now, at this meeting, among other things, you or Mr. Schuette told Mr. Huarisa and Mr. Meers about some of the negative findings that your team had made, correct?

A. That is correct.

Q. And, among other things, you mentioned that some of these negative things were the deferred costs and other items that you thought would have to be expensed off, correct?

A. That is correct.

Q. Didn't you say to them that you could not see how the deferred costs could be amortized against any production units in the future?

A. That is correct.

Q. Now, Mr. Huarisa said, as I understand it, that he thought that he could show you how these costs could be amortized in the years 1969 and 1970, is that right?

A. That is correct.

Q. And asked for another meeting?

A. That is correct.

Q. Isn't it true, Mr. Ethington, that the principal reason you gave Mr. Huarisa and Mr. Meers for terminating the negotiations was that you could not see how the SKI earnings were going to be met because of the

tremendous write-offs that were going to be faced by SKI in your opinion?

A. No, that was not the principal reason.

Q. It was not?

378 A. No, it was not. It was the number third on my list. It was one of the three reasons.

Mr. Fowle: Excuse me a moment, your Honor.

The Court: Yes.

Mr. Fowle: I seem to have gotten tangled up in my notes.

The Court: Okay.

(Brief interruption.)

Mr. Fowle: I will be referring to page 83 of Mr. Ethington's deposition.

By Mr. Fowle:

Q. Let me ask you, Mr. Ethington, whether during your deposition this question, or these questions, were put to you and whether you gave these answers—

The Court: What page?

By Mr. Fowle:

Q. (Reading:)

"Q. Was there any other topic or subject discussed —"

The Court: Do you have the page? What is the page?

Mr. Fowle: Page 83.

The Court: All right.

By Mr. Fowle:

Q. (Reading:)

"Q. Was there any other topic or subject discussed at the January 20th meeting other than what

379 you have generally referred to as deferred costs and other items to be expensed?

"A. We talked about products and new developments and the business in general, and that we did

not think that we were going to get the synergism we originally thought, and there were various reasons, but basically, that we did not see how the earnings were going to be met because of the tremendous write-offs that were going to be faced by Standard Kollsman in our opinion."

Now, were those questions put to you and did you give those answers?

A. Yes, I did.

Mr. McSweeney: If the Court please, I am going to move to strike that as far as impeachment because that doesn't contradict —

The Court: Well, what do the words "but basically" mean?

Mr. McSweeney: I don't know. It's just the word "basically" —

The Court: Well, at least the answer may stand.

* * *

382 Q. Yes. And this, again, was a two- or three-hour meeting, was it not?

A. I think some period of time like that.

Q. And was it Mr. Schuette who talked on the subject of synergism or the lack of synergism at this meeting?

A. Yes, it was.

Q. And you, again, expressed a lack of confidence in SKI's earnings forecast, did you?

A. Yes, I did.

Q. And Mr. Erickson, I believe, spoke on the subject of preproduction costs, did he not?

A. Yes, he did.

Q. And questioned the likelihood of SKI's being able to amortize these costs over future production?

A. Yes, that is correct.

Q. And Mr. Ryan — you remember who Mr. Ryan was?

A. Yes, I do.

Q. I guess you identified him as the chief financial officer of SKI?

A. I believe that that was his title at the time.

Q. Mr. Ryan attempted to show you or show you and the others at Sundstrand how it would be that these costs, these deferred preproduction costs, could be deferred, could be charged off or expensed off against production in 1969 or 1970, is that true?

383 A. Yes, that they would be amortized, I believe is the word that he used.

Q. That they would be amortized in 1969 or 1970?

A. That is correct.

Q. But neither you nor Mr. Schuette were persuaded by what Mr. Ryan had to say?

A. We had no reason to doubt him but we just didn't know how they could do it.

Q. You had your own ideas?

A. I had my own ideas.

Q. And, at the close of the January 22nd meeting, you and SKI people agreed to make a public announcement that the negotiations had been terminated?

A. That is correct.

Q. And this was done?

A. That is correct.

Q. And, as I understand it, at this meeting Mr. Meers and Mr. Huarisa advised you that they would continue to search for a satisfactory merger partner?

A. That is correct.

Huarisa Deposition Testimony

213 Q. So the next contact on this matter was your meeting that evening with Mr. Ethington and Mr. Schuette?

A. Right.

Q. And according to your calendar pad that was in the Oxford Room of the Sheraton-O'Hare, is that where it was held?

A. Yes, sir.

Q. At six-thirty p.m.?

A. Yes, sir.

Q. Who was present?

A. Mr. Schuette, Mr. Ethington, Mr. Meers and myself.

214 Q. Okay; what was said at that meeting?

A. I think — I don't know whether Mr. Ethington or Mr. Schuette stated that they felt, number one, they were worried about the write-offs; they had pencil sketches of the write-offs, and I don't remember what they were. They felt that there wasn't enough new products in the Avionics Division that would help them in the aircraft industry; and third, that they felt that sooner or later we would get a nationwide bargaining and their rates were so much higher than ours that we would lose some of our profit potential.

Q. Labor rates?

A. Right.

Q. What else?

A. That's about the point of it.

Q. What did you say?

A. I told him that I was not prepared; if they had told me that that is what they wanted to do I would have brought figures of what they wanted in the way of that, and I recommended that we meet with Ryan so we could come back up to the figures that they were throwing at me.

Q. Did you have any figures there with you
215 that day?

A. No, I did not.

Q. What else did you say?

A. And they agreed to have a meeting a couple of days later, or the next day.

Q. What did Mr. Meers say?

A. I don't recall what he said.

Q. What write-offs did they say they were worried about?

A. I don't remember. They had a figure, but they were worried — I guess they were worried about all of them.

Q. Well, as of that time you hadn't taken any write-offs, had you?

A. But they had made a complete study, they knew as much as we did on it, they went through our entire books, they questioned everything in the write-offs; they knew as much as we did in write-offs; that if we didn't get the orders we would have to face the write-offs. They got all of that from our books.

Q. What did you tell them about the write-offs?

A. I said that we would have to sit down with somebody who knows more of the details than I do, and we would discuss it with them.

* * *

219 A. I didn't discuss it with anyone; I might have brought Neil Kennedy up-to-date, but I don't recall that I had; and I am sure that I called Ryan the next day and said "Will you get all the figures together and see what you have given Sundstrand, and let's break it down and see if they have got the same figures we have."

Q. Was Mr. Ryan then in New York?

A. No.

Q. Out here in the Chicago area?

A. Right.

Q. All right. So you had, then, another meeting with the Sundstrand representatives?

A. That's right.

Q. On the 20th, did you make the date for the next meeting?

A. I think we did.

Q. And that was on January 22nd, was it not?

A. That's correct.

220 Q. All right; who was present at the meeting on January 22nd?

A. Mr. Schuette, Mr. Ethington, Mr. Erickson, and I think Mr. Miller, Meers, Ryan and myself.

Q. That meeting was at the Chicago Club?

A. That's correct.

Q. Before going to that meeting, did you confer with Mr. Ryan as to what he was going to say or what he was going to present to the Sundstrand representatives?

A. Well, I asked him if he had all his figures in the write-offs and the labor figures, and if we had any of their labor figures, which he did, and
221 that's about it. I told him what to expect.

Q. And did you tell him that your view was that the points that Sundstrand made were not well-founded and you wanted to demonstrate to them why they were not?

A. Yes, basically that's it.

Q. All right.

Now, at the meeting, what was said and by which person?

A. Well, we took point by point, and they took job by job; Mr. Ryan and Mr. Miller reviewed them, I guess, with the help of Ethington and Schuette.

Q. You were there, too?

A. Yes, sir.

Q. Well, what jobs did they take?

A. They took all of them that they had brought up — I can't tell you which they are, every one that Mr. Ethington questioned was brought up.

Q. You mean Mr. Ethington enumerated specific jobs which he questioned?

A. I don't know whether they were specific jobs or specific dollars that he questioned.

Q. Well, in other words, you mean at the meeting on January 22nd Mr. Ethington questioned either
222 specific jobs or specific dollars?

A. That's correct.

Q. What do you mean by questioning specific dollars?

A. The amount of dollars that he figured we would have to write off.

Q. I see. Which ones — do you recall now as to what Mr. Ethington said?

A. He said that he had no confidence that we would get these jobs and we would be faced with a write-off.

Q. All right. Which ones did he name?

A. All of them that he had on his list. I can't tell you which ones they are; they were all of them.

Q. All that Mr. Ethington had on his list?

A. Yes.

Q. He had a list there?

A. Yes, he did; or Miller had a list: If it was Miller, I am not sure.

Q. Did you see the list, did he show it to you?

A. Yes.

Q. You read it?

A. I am pretty sure I did.

223 Q. You don't recall which jobs?

A. I said all of them that they question, and I turned it over to Ryan to answer them one at a time.

Q. Well, the list had all that they questioned, but what I want to know is what was on the list?

A. I don't know.

Q. You don't know?

A. No.

Q. Did you listen while Mr. Ryan explained to them why they were wrong?

A. Yes.

Q. You agreed with what Mr. Ryan said?

A. He knows more about it than I do; so I would have to agree with him.

Q. You didn't contradict him?

A. Not that I recall.

Q. What do you recall that Mr. Ryan said about any specific job?

A. He pointed out to them the future, the potential, and so forth.

Q. Well, with respect to the future and the potential of the jobs, wouldn't you know more about
224 that than Ryan?

A. He has been in on it, working with the Sundstrand people and working with our people, and they have been working together on it, and I am sure the Sundstrand people asked a lot more questions than Mr. Ethington did, so I think he was well equipped to answer the questions at that time better than I was.

Q. Well, if you don't remember specifically what Mr. Ryan said, was the gist of what he said that they would not have to take these write-offs because they would get orders?

A. He said that we are trying to get the orders. If we get the orders we would not have to write them off.

Q. Did he say if you didn't get the orders how much you would have to write off?

A. I think the figures were there, yes; I don't recall that — anything specific.

Q. What else was said at this meeting?

A. That's all I can remember. We went through the labor again, we went through the future products, and I think at the last moment Mr. Ethington said that he had no confidence in our projecting our profit, and he didn't think we could earn two dollars; that I
225 remember.

Q. And what else was said?

A. That's it.

Q. Did Mr. Ryan indicate at that meeting what Standard Kollsman was expected to earn in 1968?

A. Mr. Ethington and his group had a breakdown of the $2.13 that you have a copy of.

Q. Well, that was for 1969, wasn't it?

A. '69, I am sorry.

Q. I was asking if Mr. Ryan indicated —

A. Absolutely not.

Q. — on January 22nd —

A. How could he when we were trying to discuss the write-offs?

Q. I don't know. I just asked the question, either he did or he didn't.

A. I am trying to put a logic to it.

Q. Well, did he indicate since this was the 22nd day of January, 1969, what your company expected to earn for 1968?

A. No.

Q. What did he say about how long you were going to wait before you determined whether to take the write-offs as of 1968?

226 The Witness: I think I answered that yesterday, that we would wait until we were ready to go to press, if we got the orders we wouldn't take the write-off.

By Mr. McSweeney:

Q. Now I am asking you, though, did Mr. Ryan say that in the meeting of January 22nd?

A. Not that I am aware of; he may have, but I don't know.

Q. What did Mr. Meers say at this meeting?

A. He mostly listened; I don't think he said much of anything.

(9) On January 23, 1969 it was announced publicly that merger negotiations were terminated

Ethington Trial Testimony

144 Mr. Meers stated that he did not think that the earnings were that important. I told him that I thought earnings were very important in a merger.

After Mr. Ryan and Mr. Huarisa had presented this, I had a written statement with me that I had tried to summarize: the reasons for calling the merger off. I had them in my notebook written out. I read those reasons. Basically as I can remember them, I read that the first reason for calling the merger off was some labor problems that we would have relating to the union; No. 2, the synergism of the two operations was not there; No. 3, that I was not comfortable with Standard Kollsman's ability to amortize these costs.

With that in mind, with those reasons, Sundstrand did not want to proceed with the merger.

Mr. Meers then stated that he would continue to work on effecting a merger for Standard Kollsman with other people. Mr. Huarisa also stated that he was working on a potential merger with another company.

Right now I can't recall anything more at that meeting.

Q. Well, did you respond to Mr. Huarisa's and Mr. Meers' statements that they were working on other mergers?

A. I said that we would be happy to cooperate and have our stock participate in the merger.

Q. What do you mean by have your stock participate?

A. Well, we had purchased a block of 223,000 145 shares of stock from Mr. Huarisa.

Q. Have the stock of SKI go into the merger, is that it?

A. Yes. It was now Sundstrand's, Sundstrand's SKI stock.

Q. Did you then announce to the public the calling off of the merger?

A. Yes, we did.

Q. When was that?

A. I believe it was done the next day but I am not positive.

The Court: I think this is probably a good time to recess unless you have got — what do you have, another notebook?

Mr. McSweeney: Just corroborative of that.

The Court: All right. Let's postpone that.

Mr. McSweeney: Sure.

The Court: Let's find out tomorrow morning when you gentlemen come in — I established a halfway precedent today but that is all it is — as to why there are not this type of evidence is corroborative and whether it is proper or not.

Mr. McSweeney: Yes, your Honor.

The Court: So, let's postpone that ruling until tomorrow.

Gentlemen, I don't want you sitting here each morning while I have some motions to dispose of. On the other hand, I don't want to be waiting for you when I get through with

IV. ETHINGTON AND SADLER DIVEST THEMSELVES OF THEIR SKI STOCK

Ethington Trial Testimony

364 Q. Well, at about what time did he say this to you?

A. Some time in the middle of January.

Q. Didn't Mr. Miller advise you when he returned from New York — he was part of the team that was down in New York that week of January 7th, wasn't he?

A. I don't remember if Mr. Miller went to New York or to Elmhurst. I would have to check which one he went to.

Q. Didn't Mr. Miller tell you when he got back from New York —

A. I don't think he was in New York, sir.

Q. I may be wrong about that, Mr. Ethington.

A. I think you are.

Q. My co-counsel says that Mr. Miller didn't go to New York. So, let's forget that.

Hadn't you, yourself, in the middle of January begun to develop some questions about the wisdom of this acquisition of SKI?

A. In the middle of January, I did.

Q. I mean, on January 14, 1969, you placed an order with your broker to sell the 2,000 shares of Standard Kollsman stock that you had bought on December 27th, didn't you?

A. That is correct.

Q. Mrs. Ethington sold the few shares that she had on January 17th, didn't she?

365 A. I think that I sold those.

Q. Do you know whether Mr. Sadler owned any stock, SKI stock, in the middle of January?

A. I think in the middle of January, I knew that he did.

Q. I mean, do you know that he sold 1,000 shares of SKI stock on January 17th?

A. No, I do not, or did not.

Q. I hand you, Mr. Ethington, two documents marked Defendant Sun-Huarisa Trial Exhibit 20-A and 20-B for identification, purporting to be confirmations from Bear, Stearns & Company of sales on the account of you and Mrs. Ethington of SKI stock on January 14, 1969.

I ask you if you can identify them for me?

A. Yes, I can.

Q. Will you tell me what they are, please?

Are they what they purport to be?

A. Yes, they are.

Q. The whole survey team, the whole SKI survey team had a meeting on the morning of January 20, 1969, is that right?

A. I believe that is correct, sir.

Q. Were all of the members there so far as you know?

A. I do not know. I was not at the meeting.

Sadler Trial Testimony

479 By Mr. Freehling:

Q. Mr. Sadler, you recall, I am sure, that you had the pleasure of testifying in this case once before at the trial then before Judge Hoffman. Do you remember that?

A. Yes, I sure do.

Q. At page 1919 of the transcript, you were asked the following question and you gave the following answer:

> "Q. What was the date of your conversation or conversations with Mr. Schuette and Mr. Ethington upon your return to Rockford?
>
> "A. The 13th of January, 1969."

Do you recall that?

A. Yes, I do. You have tossed in Olson. That is my problem. I don't know if he was there or not.

Q. I see. Well, I am sorry.

You reported to Mr. Ethington and Mr. Schuette on January 13th, 1969, is that right?

A. Yes. No question about that. Yes.

Q. I am sorry. It was at that report or discussion with Messrs. Ethington and Schuette at least that you talked about your doubts about Standard Kollsman, is that right?

A. Yes, I am sure I did.

Q. And your disappointment?

A. Yes.

Q. Then on January 17th you went out and sold 480 1,000 shares of your Standard Kollsman stock that you owned for your personal account, isn't that right?

A. Yes, that is right.

Q. After first showing it to your counsel, I show you Defendant Sun-Huarisa Trial Exhibit 36-A and -B. I ask you whether those are the confirmations of your personal sale of 1,000 shares of Standard Kollsman stock on January 17, 1969.

A. Yes, that is it.

Q. On January 20, 1969, there was a meeting of the survey team, was there not?

A. Yes, there was.

Q. At that meeting Mr. Ross reported about earnings at Kollsman Instrument Corporation, did he not?

A. Yes, he did.

Q. He said there were serious questions for future earnings at Kollsman Instrument Corporation, isn't that right?

A. Well, I am sure he talked about the problems there.

When you say "serious questions," you know, I am not sure about those words but it was something like that. He certainly expressed concern about the earnings, yes. I would say that.

Q. Mr. Miller also gave a financial summary regarding the whole company of Standard Kollsman, isn't that right?

A. Yes.

V. RESPONDENTS ARGUED REPEATEDLY TO THE DISTRICT COURT AND TO THE COURT OF APPEALS THAT SUNDSTRAND OFFERED NO EXPLANATION FOR ITS PURCHASE OF THE BURKE STOCK OTHER THAN ITS UNFOUNDED BELIEF THAT IT WAS LEGALLY OBLIGATED TO DO SO

(1) Excerpts from Respondents' Pre-Trial memorandum at the first trial

5 As will appear throughout the trial, this case has some puzzling aspects. The most perplexing of all—which must await an explanation by Sundstrand—is why Sundstrand elected to exercise an option to purchase 223,190 shares of SKI stock for over $6.3 million after completing an intensive survey which reached negative conclusions about SKI's financial condition and future business prospects. Sundstrand will argue that the agreement pursuant to which the option rights were transferred from Huarisa to Sundstrand, *required* Sundstrand to exercise the option and to complete the purchase of the Burke stock. We submit that the documents attached to the complaint show on their face that this was not the case.

(2) Excerpts from Respondents' Pre-Trial memorandum at the second trial

6 Six years of litigation have failed to uncover the reasons why Sundstrand exercised its option to purchase a 10% interest in a company whose financial condition and business future Sundstrand thought so unsatisfactory. Corporate acquisition negotiations had been terminated two weeks earlier. Sundstrand was under no
7 obligation to purchase the Burke stock. The market price of SKI stock on February 6, 1969 was about $5.50 below Sundstrand's option price of $30 per share. Moreover, senior Sundstrand executives demonstrated that they did not want to own SKI stock personally. Two of them, Sundstrand's president James Ethington and its Executive Vice President Carl Sadler, had secretly bought SKI stock in late December, before news of the proposed acquisition was made public. They unloaded most of their shares in mid-January 1969, just before the public announcement that acquisition negotiations had been terminated.

(3) Excerpts from Respondents' brief in the Court of Appeals

49 It must be concluded that there is no explanation in the record for Sundstrand's purchase of the Burke stock on February 6, 1969, other than the unfounded belief that there was a legal obligation to purchase it.

(4) Excerpts from Respondents' reply brief in the Court of Appeals

13 We renew our argument (Sun-Huarisa Br. 44-49) that, except for a supposed but non-existent legal obligation, Sundstrand offered no evidence whatever as to what caused it to purchase the Burke stock on February 6,

1969, two weeks after the avowed reason for buying it had disappeared (Ethington Tr. 131, 328-338). We also renew our argument that the loss of which Sundstrand complains in this case was caused entirely by its own imprudent conduct. Sundstrand has failed to refute these arguments.

(5) Excerpts from Respondents' answer to Sundstrand's petition for rehearing in the Court of Appeals

From the very outset of this litigation Sundstrand and its counsel have asserted unequivocally that Sundstrand was legally obligated by the January 9, 1969 agreement with Huarisa to complete the purchase of the Burke stock on February 6, 1969.

• • •

Moreover, Sadler, Sundstrand's president, testified that Ethington (Sadler's predecessor as president of Sundstrand) told him that Sundstrand would purchase the Burke stock because 'our counsel feels we are obligated to buy the stock.'

As a matter of fact, the record in this case supports no explanation other than Sundstrand's mistake of law.

VI. DEPOSITION TESTIMONY CITED BY THE COURT OF APPEALS AT 553 F.2d p.1050, n.35, THAT IS IN THE RECORD ON APPEAL BUT NOT IN THE TRIAL RECORD

Ethington Deposition

559 Q. On January 20, 1969, did you discuss with anybody the Burke shares?

A. Not that I can remember.

Q. Did you say anything to Mr. Huarisa or Mr. Meers?

A. On the 20th?

Q. On the 20th about, the Burke shares?

A. Not that I can remember.

Q. Did you personally consider what, I mean upon making your decision not to go ahead with the merger, did you consider what you were going to do about the Burke shares?

A. Yes.

Q. What did you consider about it?

A. To exercise our legal document and agreement that we had made.

Q. Did you discuss that with anybody?

A. Our legal counsel.

Q. When?

A. Somewhere around that date.

* * *

565 Q. You say you went over the reasons. Will you state what you told Mr. Olson on that subject?

A. I cannot recall. I cannot recall.

Q. What did Mr. Olson say about the reasons, if anything?

A. Mr. Olson felt that if our team did not think we should go through with it, that he did not, either. And he was reasonably happy that we were not going to go through with the deal.

Q. Did he say why he was reasonably happy?

A. No, he did not.

Q. Did you mention, was there any mention in this conversation with Mr. Olson about the Burke stock?

A. Not that I can recall.

Q. Did you discuss with anybody other than Mr. Pitte as you have stated whether or not to go through

with the purchase of the Burke stock? After what
566 you had learned from the team?

A. Yes, I did.

Q. With whom?

A. I reported back to our management committee that we felt we had a legal and moral obligation to proceed with buying the stock and saw no way of breaking the agreement.

Q. When was that?

A. Some time around January 22nd or January 23rd.

567 Q. Was that a meeting of the Management Committee?

A. I don't know if it was done at a joint meeting or individually, but it was done at that time. It was not an official meeting.

Q. Did you say this to these men at one time at one official meeting?

A. I do not remember; I do not remember if they were all together at one time or if it was done separately, but they were all notified.

Q. Who was on that management committee?

A. Mr. Olson, Mr. Schuette, Mr. Sadler, Mr. Gustafson and myself.

Mr. McSweeney: Was Rothstein there?

The Witness: He is on the Management Committee, but not for this decision.

Mr. McSweeney: He said, "anyone else." We have listed these people before.

The Witness: Yes.

Mr. McSweeney: Anyone else that you know of?

The Witness: Not that I recall.

Mr. Schilling: I think you are referring to the
568 inside directors.

The Witness: That is correct.

By Mr. Kullby:

Q. You had an inside directors' meeting?

A. No, these people are called inside directors that I have named.

Q. They are employees of the company?

A. They are employees of the company.

Q. What did you say to Mr. Olson?

A. What?

Q. Do you know where you were when you spoke with Mr. Olson on the subject of the Burke stock, whether you should go ahead with it?

A. No, I do not.

Q. What did you say to him?

A. I told him that we were advised that we had to proceed with the agreement that we had made.

Q. What did he say?

A. That we would have to honor our obligations.

Q. At that point you had not spent any money on this stock, had you?

A. We had committed to spend.

Q. You had not delivered any money?

569 A. No, we had not.

Q. You had not delivered any stock?

A. No, we had not.

Q. What did Mr. Olson say?

A. I answered that question.

Q. I am sorry.

A. That we would have to honor our agreement.

Q. Was anybody else present?

A. I don't remember any. I stated previously I don't remember if we were in a group or if I did it individually.

Q. Was this before or after the meeting at the Chicago Club?

A. It was probably right after. The next day after.

Q. Did you speak to each of these men?

A. Yes, I did.

Q. You, personally?

A. Yes, I did.

Q. What did you say to Mr. Sadler?

A. The same thing I said to Mr. Olson.

Q. What did Mr. Sadler say?

A. That we would have to go ahead with the
570 deal if that is our legal obligation.

Q. Did you mention at that time or did any of these two men we have asked about so far, Olson or Sadler, or any mention at those conversations about the market price of Standard Kollsman stock on January 22nd or 23rd?

A. Not that I can recall.

Q. Do you recall what the market price was?

A. No, I do not.

Q. You did not take that into account in your thinking on that subject?

A. It would not have made any difference. I had a legal obligation so the market price of the stock at that time could have no influence over what I had to pay for the stock.

Q. You use the words "moral obligation." What do you mean by that?

A. Legal and moral, I said.

Q. Yes, what do you mean by "moral obligation"?

A. We had made a deal with Mr. Huarisa and because we were interested in the merger that we would buy the shares of stock. And we signed a legal agreement to do so. And we made a commitment to him that
571 the reason we were going to buy this is that we were going to proceed with the merger and in good

faith, thought it was going through. And I consider this a moral obligation.

Q. To utilize Sundstrand's funds to buy something which already was a million and a half dollars less than $30 a share?

A. This part was a legal obligation.

Q. Whose moral obligation?

A. I felt a moral responsibility. I am sure the integrity of our other officers probably would, too, but I cannot answer for them.

Q. What did Mr. Schuette and you talk about on the subject of the Burke stock?

A. The same thing. That we were committed to buy it legally. I can say that I was not happy.

Mr. McSweeney: He has got a luncheon engagement, but he will be back.

The Witness: But I will be back by two.

(Deposition continued to the hour of 2:00 o'clock, of the same day, Friday, October 31, 1969.)

573 JAMES ETHINGTON, having been previously sworn, resumed the stand and testified further as follows:

Cross Examination (resumed)

By Mr. Kullby:

Q. Before we recessed for lunch, Mr. Ethington, we were talking about moral and legal obligations. Who did you feel you had a moral obligation to?

A. Mr. Huarisa.

Q. To whom did you feel you had a legal obligation?

A. Mr. Huarisa.

Q. It was not Mr. Huarisa's stock you were buying, was it?

A. Yes.

Q. Mr. Huarisa was not going to make any money on that. You knew that, didn't you?

A. Yes.

Q. So what moral obligation did you feel you had to Mr. Huarisa?

A. A moral obligation. I think I testified already to that, is that we had committed to tentatively plan
574 to go ahead with the merger. So this stock then became a part and parcel of that merger and therefore I felt that this was part of the total package.

Q. But you called off the merger?

A. I called off the merger and—after we had committed to buy the stock.

Q. So you thought you had a moral and legal obligation to Mr. Huarisa to spend six some odd million dollars of the company's money on something that was worth much less than that on the day you paid the money?

A. I don't think it was worth much less than that on the day we decided to continue to exercise the agreement.

Q. You say you read the Wall Street Journal every day, isn't that right?

A. Yes.

Q. You check the stock price on Sundstrand, do you not?

A. I tried to.

Q. At this time you were vitally interested in Standard Kollsman, were you not?

Olson Deposition

34 Q. Are you talking in the area when it was decided not to go forward with the acquisition when they reported reasons?

A. Whenever that was, when we decided not to go forward with the acquisition, one of the reasons was lack of confidence, their ability to predict with any accuracy, the lack of these other things that I have mentioned—many of the problems.

I might say we did have and still do have some confidence in ourselves to take something and prove it. That's part of acquisitions.

Q. In the context of conversations of deciding not to go forward with the acquisition, what conversation, if any, did you have with any Sundstrand personnel about the shares of stock?

A. We had a legal obligation to buy the stock.

Q. Who told you that?

A. Ethington.

Q. He told you that you had a legal obligation to pay six million dollars?

A. Yes.

Q. Who did he say told him that?

A. I don't know that. I presume our lawyers.

Mrs. Hall: Would you read that response?

(Answer read.)

By Mr. Kullby:

Q. Didn't they show you the papers which are attached to that agreement that you don't have to pay anything more after you pay the down payment? Did the lawyer point that out to you?

A. I don't think so.

Mr. Montgomery: You mean did he point out the pages of the agreement?

Mr. Kullby: I am asking him whether he had any conversation where anybody pointed that out to him.

The Witness: I don't think I understand your question.

By Mr. Kullby:

Q. I am asking whether you had any conversation with Ethington, or Schuette, or whoever you had any conversations that—

A. That we didn't have to buy the stock?

Q. You said you had a legal obligation to pay six million dollars of the company's money.

A. That's right. We didn't know the whole effect of this thing at that time. You understand, we
36 would have probably abrogated the agreement and take the chances of being sued had we known what we know now.

Q. And if you had no chance of being sued for not—

A. I don't know.

Q. —not going ahead with the payment of six million dollars, would you have not paid it?

Mr. Montgomery: It is a hypothetical question, "wouldn't have any chance of being sued."

The Witness: I don't know.

By Mr. Kullby:

Q. Who did you have conversations with about chances of being sued for not paying the six million dollars?

A. I didn't say I did, did I?

Q. I thought you indicated that you were told that you had a legal obligation.

A. That's right. I was—it was so presented to the board. I don't know what the minutes say. We still felt the stock was—while we didn't think we were going ahead with it, we thought it would be all right.

Q. You say it was presented to the board that
37 you had an obligation?

A. I'm sure it was.

Q. To pay the entire six million dollars, in excess of six million dollars?

A. Whatever it was, whatever the payment was.

Q. Who said that?

A. I would presume that Schuette presented it, his recommendation to the board.

Q. Had there been a board of directors' meeting?

A. There was one in February sometime.

Q. Between January 8, when you had the conversation over the telephone with Mr. Ethington, on February 14—

Mr. Montgomery: I think that the date of the conversation was January 6.

By Mr. Kullby:

Q. Okay, January 6. I didn't mean to put—

A. I don't think there was an official board meeting, but there was a polling of the board.

Q. About which you told us?

A. Yes.

Q. And the first board meeting was the one on February 14.

38 A. I presume that's correct.

Q. I take it you were present at that meeting.

A. Yes.

Q. Would you tell us to the best of your recollection what was said about the purchase of the stock, the Standard Kollsman stock at the board meeting of February 14, and who said it?

A. I don't remember any detailed comment on it. See "Mr. Schuette reviewed the background associated with the preliminary acquisition discussions on S.K.I. and the reasons for not proceeding with acquisition."

Q. Did he say what the reasons were?

A. I'm sure he did. Didn't you talk to him?

Q. I'm asking what you remember, Mr. Olson.

A. I don't remember what he said. I'm assuming he gave a reason.

Q. Did he reiterate what Mr. Miller had previously told you about?

A. I don't remember what he said.

Q. What he thought the earnings of Standard Kollsman would be?

A. If he had them, he would have presented—

* * *

40 Q. Well, do you recall their reporting to you about what they were going to tell Huarisa when it was decided that you were not going to go through with the acquisition?

A. I don't recall. I presume they did report. I'm sure they told me that. They asked my advice and that sort of thing, but—

Q. Did any of the board members ask you questions as to—at the February 14th board meeting—

A. If they are not recorded, I don't remember if they did or didn't.

Q. Before that board meeting, did you have any conversation with anybody about whether or not the Sundstrand check should be issued—

A. I presume—

Q. —in excess of six million dollars for these Standard Kollsman shares?

A. Oh, I'm sure we discussed our legal obligation, and I don't know when and I presume it would be with Schuette and Sadler and Ethington.

Q. Do you know when the check was issued?

A. No.

Q. Did you have any discussions with Mr. Swanson about.

* * *

68 The Witness: Take two or three days there, because sometimes out of town and I'll call again.

Mr. Schilling: Do we get an internal record of that?

The Witness: No. I write a memo.

Mr. Schilling: No. I mean does your switchboard?

The Witness: None. I don't know.

Mr. Schilling: I don't know. I'll check that.

Mr. Montgomery: Off the record.

(Discussion had off record.)

By Mrs. Hall:

Q. Mr. Olson, I believe you testified that at some point in time Mr. Ethington told you that Sundstrand had a legal obligation to pay for this block of stock.

A. Yes.

Q. Did you question him about that statement?

A. I don't recall. It may seem funny, but we don't question each other on things like that. Thirty years of a good record kind of . . . you know. I think a new person I would question.

Q. I believe you made a statement to the effect that
if you had known the whole effect at the time,
69 you might not have paid the money but you might
have—

A. Risked the lawsuit. Of course, that's hindsight. I would go to our attorneys and see what—what our position was.

Q. But you didn't do that at that time?

A. No, I did not.

Q. And why didn't you?

A. Because I didn't know about this subsequent Ernst & Ernst report.

Q. So the thing which you didn't know at that time was the Ernst & Ernst report?

A. That was the major thing we didn't know and we didn't know anything else continued to—let's see. The earning statement came out in April, I believe, for '68, which was different than what we had been led to believe.

Q. Anything else?

A. I don't think anything else. I think they are the basic things.

Q. You said that you looked at portions of the depositions of Mr. Ethington and Schuette.

A. Ethington primarily.

Q. Anyone else?

A. No, I don't think so.

Pitte Deposition

96 A. Yes, there was. Mr. Kennedy had indicated that he did not know where in the event of a fight, he did not know where some of these blocks would end up, on which side.

Q. Anything else on the subject of blocks favoring or opposing the merger that you can recall?

A. No, I don't know.

Q. You stated, according to my notes, Mr. Ethington concurred in the advice that you gave him, namely, giving serious—well, I guess giving serious consideration in bailing Mr. Huarisa, is that correct?

A. That's correct.

Q. Is that the advice that Mr. Ethington concurred in?

A. Yes, sir.

Q. And Mr. Ethington said that someone should proceed to work out the details, is that correct?

A. That's right. He and I then told—suggested that —I don't know whether it was I suggested it, but certainly if I didn't, that it was with my concurrence—

97 I think I suggested Mr. Kennedy or he suggested that his office would undertake the first draft and that we would hopefully get the first draft before the close of business that day?

Q. You stated, according to my notes, that there was no question at that meeting, but Sundstrand was going to pay out 6.6 million dollars to acquire the Burke stock, is that right?

A. That's right.

Q. And you said that you stated at the meeting that it was important that Mr. Huarisa give notice to the Burkes or their agent that he was exercising his option, is that correct?

A. That is correct, but because this was part and parcel of this problem of assignability.

Q. Is that something that was said at the meeting?

A. Yes, sir.

Q. Do you recall anything more said on the subject of why it was important that Mr. Huarisa should give that notice?

A. Well, I irrated quite a bit on that. I think I gave that testimony this morning.

Q. I am only asking for testimony you haven't—

* * *

116 to assume on the law of averages and in view of our past practices that we probably were going to go through with the merger.

We then pointed out that the stock at that time of Standard-Kollsman was over $30 a share on the New York Stock Exchange and we reviewed the fact that there obviously was interest on the part of others in Standard-Kollsman. Standard-Kollsman could be recognized as a target for a takeover bed and we related—to buttress this point, the conversation we had with Messrs. Kennedy and Huarisa that morning to this effect.

We then said that if contrary to our past practice our survey made us determine to back off of the acquisition

and that unlikly event of what our risks at that point.

We then decided—we then argued that those risks were minimal in view of the fact that if we publicly stated that we were no longer interested in proceeding with the merger after the survey deemed be reported back and there had been a management determination to that effect. That it was altogether probable that one or more of these other companies,
117 who had evinced some interest would proceed almost immediately to make their move to take control of this company and that accordingly with the stock up at its present posture the possibility that we were running any substantial risks in acquiring the stock at this time, if we later did not decide to proceed with the merger were minimal because we in turn as a stockholders of Standard-Kollsman, a 9.8 percent stockholder would be taken out of one of these other companies without a financial loss to Sundstrand.

After a great deal of discussion between the six of us on the phone, this presentation met with the approval of the other four and Mr. Olson as chief executive officer and chairman of the board was requested to contact immediately the other four outside directors on the telephone and inform them of our, of the stand of the inside directors in this regard.

That is pretty much it.

Q. Do you have any further recollections at this time of your conversation during that telephone call that you have not already related?

A. No.

• • •

167 By Mr. Freehling:

Q. Let me ask you this: Did you advise Mr. Sacks as of January 22, or thereabouts— Maybe I should strike that and ask you:

Can you tell us approximately when your conversation was with Mr. Saeks that we have been discussing?

A. Approximately January—approximately January 22.

Q. All right. Now, in your conversation with Mr. Saeks on or about January 22, 1969, was anything said to him concerning Sundstrand's commitment to acquire 223,000 shares of Standard Kollsman stock in light of the fact that the merger negotiations had been terminated?

Mr. Montgomery: Well, I object to the form of that question because it assumes that at that point in time Sundstrand had a commitment rather than a finalized purchase of this stock. To that extent it misstates the record.

Mr. Freehling: Well, let's find out whether any-
168 thing was said concerning the commitment.

By The Witness:

A. Mr. Saeks was very definitely informed that there was no change in the part of the prior submission, which is Defendants' Exhibit 205, relating to the 223,190 shares. There was no change in that—of course what I am saying is that he was fully apprised that when the merger was scrubbed, this did not scrub anything relating to that block of stock.

By Mr. Freehling:

Q. Was he told anything in this conversation on or about January 22, 1968, as to whether the purchase by Sundstrand of 223,000 shares of stock had been completed?

A. I don't recall.

Q. You testified last time that during the—this is at Page 140 of your testimony—that during the week of January 13 you had a conversation with Mr. Kennedy concerning the January 9 agreement and concerning dis-

closure of it, and you said that, quote, "A copy of this—" and I am not absolutely sure what "this" is—

• • •

171 Q. Do you know when they became effective?
A. January 24, 1969.

Q. Now, I believe you testified that the next event involving you and the Sundstrand-Standard Kollsman matter and which fits within the guide lines set by your counsel as to matters on which you may testify, was on February 3, 1969, is that correct?

A. That's correct.

Q. What happened on February 3, 1969?

A. I had one or more telephone conversations with Mr. Hart of Pope-Ballard.

Q. Was anyone else on the line, to the best of your knowledge?

A. No, they weren't.

Q. Were you in your office during those conversations?

A. Yes, sir.

Q. Would you tell us, please, to the best of your recollection what you said to Mr. Hart and Mr. Hart said to you?

A. I believe I pointed out that under the 1967 pooling agreement between Mr. Huarisa and various members of the Burke family, by operation of the 30-day
172 right of first refusal, an additional sum on the purchase price had to be paid by the, I believe, 9th of February, or the 8th of February it must have been. In any event, it was 30 days after the payment of the 5 percent by Mr. Huarisa on, I believe, January 8. I talked to Mr. Hart in Mr. Kennedy's absence. He was on vacation in California, and Mr. Kennedy somehow had gotten to me—I don't recall—the fact that in his absence I should talk to Mr. Hart.

In any event, I reviewed with Mr. Hart what we had determined, in light of other circumstances, previous circumstances, that we had always planned to pick up the entire—or pay down the entire remaining amount, inasmuch as we felt that the matter should be kept as secret as possible from Sun Chemical and the Burke family. This goes back to the assignability point which I mentioned in my prior session.

I also told Mr. Hart that basically we certainly did not want to be left in a position, if we only paid down what was required—and I believe that was about $1,200,-000. Don't hold me to that, but it was around that
173 figure. I believe, according to the pooling agreement—that if we just paid that amount, that it was very possible that there could be subsequent litigation by either Sun Chemical or the Burke family, working together or separately, to claim the 30-day right of first refusal which had ostensibly been exercised by Mr. Huarisa, was void, and that accordingly, if we had only paid one million two into the escrow, in accordance with the payment schedule of the pooling agreement, we really had nothing to show for it, and I thought this was a very dangerous thing, both from the standpoint of Sundstrand and for the purposes of Mr. Huarisa, who very definitely did not want to have these shares in any way in the hands of opposing parties.

I was stating this to Mr. Hart only because he was not too aware of the background, because I don't believe he had been really involved—at least I wasn't aware that he was involved—prior to the time he was substituting for Mr. Kennedy.

I desired that we work out a system to complete the transaction that week, and in view of all the background and circumstances, of course,

• • •

180 a half. It was on the second floor grill, and we, incidentally, bumped into Mr. Meers.

Q. Give us your best recollection of what was said at the luncheon meeting between yourself, Mr. Ethington, and Mr. Huarisa on February 10th, 1969.

A. Mr. Ethington and I explained to Mr. Huarisa Sundstrand's position with respect to the 223,190 shares that we had purchased from him.

While there was a great deal of talk at this luncheon, we—to summarize what we said—

Q. Well, please give us your best recollection if that is all you have.

A. I am. I am. I am.

I predicated this on the fact that there was a great deal of discussion. I mean, we hardly had time to eat we were talking so animatedly. Mr. Ethington and I told Mr. Huarisa that we were not in the business of buying stock interests of a company which had no relation to any proposed future merger into Sundstrand.

We stated that we felt a moral obligation to Mr. Huarisa, in view of all the circumstances, to hold onto this stock, but no longer than it was necessary,
181 since we had better uses for the funds.

We specifically stated that we already—Mr. Ethington stated that he already had been telephoned by a broker in the East—I believe it was Goldman, Sachs, but I am not certain—asking whether Sundstrand would be interested in selling this block. This was on the prior Friday, apparently, and that he had stated that the company at this point was not interested in disposing of those shares.

However, Mr. Ethington made it very plain to Mr. Huarisa that we were only holding these shares in order to give Mr. Huarisa time to effectuate a merger with another party, which would be a party satisfac-

tory to Mr. Huarisa and the management of Standard Kollsman, and in view of the fact that Sun Chemical now, on record, held about the same size block as Sundstrand, we recognized that Mr. Huarisa probably would have to move rapidly. We did not give him a time limit other than to say that we felt that we wanted to move this stock as soon as possible and in no event later than March 31.

Schuette Deposition

304 Q. Let's try it over again. On February 6 there was a payment made by Sundstrand for the Burke family stock, is that right?

A. That is correct.

Q. When did you learn that payment was going to be made?

A. After it had been made.

Q. Were you consulted as to whether it should be made on January 6?

A. Yes.

Q. And not thereafter until February 6?

A. That is right.

Q. You can recall no conversation with Mr. Ethington between January 6, after the January 6 telephone call and prior to February 6 concerning whether Sundstrand should go ahead and make the payment?

A. As far as I was concerned we had made the

305 commitment and we were going to carry it out.

Q. My question to you, sir, was: Did you have any conversation with Mr. Ethington on that subject after January 6 and before February 6?

A. I don't remember.

Q. Do you recall the amount of the payment on February 6?

A. Approximately $6,000,000 plus.

Q. Did you sign the check?

A. No, sir.

Q. Do you know who did?

A. No, sir.

Q. Do you know if it was paid by check?

A. It is in our Complaint. I don't know.

Q. Sir?

A. It is in our Complaint. I don't know how it was paid specifically. It is in our Complaint.

Q. Well, is it possible at Sundstrand that a $6,000,000 check could be paid for securities without your approval?

Mr. Montgomery: What do you mean, is it possible that it could be? I object to that question. It is
306 ambiguous.

By Mr. Freehling:

Q. You did not give your approval on or about February 6 to the payment of the $6,000,000, is that correct?

A. We approved the transaction and the transaction was made.

Q. Was there any discussion at any directors meeting or any management committee meeting between January 6 and February 6 concerning the payment of the $6,000,000?

A. Not that I specifically remember.

Q. Were you aware on February 6 that it was not necessary to pay the entire $6,000,000 on that date in order to continue to comply with the terms of the agreement?

Mr. Montgomery: Go ahead and answer.

The Witness: Will you read the question.

(Question read by the reporter.)

By The Witness:

A. No.

Q. Are you aware of that today?

307 A. Yes.

Q. When did you become aware of that?

A. I don't remember.

Q. Approximately, give us your best recollection.

A. Sometime after February 6. That is the best I can remember.

Q. Do you remember from whom you heard it?

A. Mr. Ethington and Mr. Ross.

Q. What did they say to you?

A. What did they say to me?

Q. Yes, sir.

A. Just that these were the terms of the agreement and this is what we had to do.

Q. Did they tell you it was not necessary to pay the full $6,000,000 on February 6 in order to protect your rights?

A. Not specifically, no.

(Here follows discussion off the record.)

By Mr. Freehling:

Q. Now let me see whether this refreshes your recollection.

308 A. All right, refresh my memory.

Q. Mr. Ethington testified according to my notes, and I am not now quoting verbatim, this is pages 579 to 583 somewhere, "Between January 22nd and February 6th I had several conversations with Messrs. Schuette and Sadler concerning the purchase of Standard Kollsman stock."

Do you recall any of those conversations, sir?

A. Yes, sir. And they all related to this $30.00 a share and the number of shares, yes.

Q. Did they relate to whether or not to go ahead with the purchase?

A. No. We had made the commitment. We are honorable people.

Q. What commitment had you made, sir?

A. That we were going to buy the stock.

Q. When was such a commitment made?

Mr. Montgomery: If you can recall.

By The Witness:

A. I can't recall.

Q. You don't recall when the commitment was
309 made to acquire the stock?

A. I know when the telephone conversation was made, which was on January 6, but when the specific commitment was made, I was not there. I don't know.

Q. Did you discuss with Mr. Ethington whether you had a commitment to purchase the stock?

A. Yes.

Q. Was that during the period January 22 to February 6?

A. Yes.

Q. Did you ask Mr. Ethington whether you had a commitment?

A. Yes.

Q. What did he say?

A. Yes, we did have a commitment.

Q. Did he show you any document?

A. No.

Q. Did you ask to see any?

A. No.

Q. Did you ask Mr. Sadler whether Sundstrand had a commitment?

A. No, sir.

310 Q. Did you discuss the subject of whether Sundstrand had a commitment with anyone other than Mr. Ethington?

A. No.

Q. Who said that there was a commitment; was that Mr. Ethington?

A. Mr. Ethington.

Q. Can you tell us when that conversation took place, to the best of your recollection?

A. Shortly after he returned from his meeting on the 6th.

Q. What meeting was that? Oh, January 6?

A. January 6, yes.

Q. Did he ever say it again to you prior to February 6?

A. Say what?

Q. That Sundstrand had a commitment to purchase the stock?

A. Yes.

Q. When did he say it to you?

A. A number of times in a number of conversations.

311 Q. How many conversations, would you guess?

A. We talked to each other every day.

Q. On the subject of whether or not Sundstrand had a commitment to buy 223,000 shares of Standard Kollsman stock?

A. I have no idea how often he made that statement.

Q. Was there anyone else you talked to on the subject of whether or not Sundstrand had a commitment to purchase the Standard Kollsman stock? This is all prior to February 6.

A. I am sure that we discussed it in the corporate group continuously, but no specific date. After we made the commitment on January 6 we felt we were obligated to carry through.

Q. Did anyone tell you you had a legal obligation to purchase the Standard Kollsman stock? Did you ask anyone whether you had a legal obligation?

A. No, sir.

Q. Would it have influenced your thinking if you had found out you did not have a legal obligation?

Mr. Montgomery: Well, I am going to object
312 to that and advise him not to answer. That is purely a hypothetical question.

The Witness: I won't answer.

By Mr. Freehling:

Q. Were you aware of the price of Standard Kollsman stock at the time of the payment of the $6,000,000?

A. Reasonably so.

Q. Do you remember approximately where it was?

A. No.

Q. Do you remember whether it was above $30.00?

A. It was below.

Q. Do you remember how far below?

A. No.

Q. Did you ever discuss with any of the outside directors prior to February 6 whether Sundstrand had a legal obligation to purchase that stock?

A. No, sir.

Q. Do you know if anyone else did discuss that
313 subject with the outside directors?

A. No, sir.

Q. Prior to February 6?

A. No, sir.

Q. No, you don't know?

A. No, I don't know.

Q. You testified this morning about a board meeting on February 14, 1969, do you recall?

A. Right.

Q. You said that Mr. Ethington made some statements about a take-out?

A. That is right.

Q. And will you tell us what those statements were by Mr. Ethington?

Mr. Montgomery: Well now, he has been asked several times—

The Witness: I have already testified to that.

Mr. Montgomery: —about what Mr. Ethington said about that and I think he has repeated it a couple of times.

Mr. Freehling: I would like to have . . .

IN THE

Supreme Court of The United States

OCTOBER TERM, 1977

No. 77-255

SUNDSTRAND CORPORATION,

Petitioner,

vs.

SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., Executors of the Estate of John B. Huarisa,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

REPLY BRIEF OF PETITIONER

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REPLY BRIEF OF PETITIONER

The Brief of Respondents in Opposition totally fails to address the legal issues presented by the petition of Sundstrand Corporation ("Sundstrand"). In attempting to shore up the faulty reasoning of the Court of Appeals, respondents beg the question of the correct analysis of causation in actions under Rule 10b-5 and never address the conflicts among Courts of Appeals with regard to each of the questions presented by the petition.

Respondents characterize Sundstrand's decision to purchase the SKI stock as a "mistake of law," glibly seeking to

dispose of petitioner's fundamental causation argument by misusing a term of art* and ignoring petitioner's legal arguments. Specifically, respondents never address petitioner's argument that even if Sundstrand had relied upon an erroneous legal opinion (*but see* Petition, pp. 20-22) there would have been no such error if respondents had disclosed the truth to petitioner. (Petition, pp. 13-17) If the truth had been disclosed, petitioner would have recognized that under Section 29(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78cc(b)) it could not have been under any obligation to consummate the transaction.

There is ample evidence supporting the District Court's finding that Sundstrand purchased the SKI stock not as a "mistake of law," but in reliance on respondents' repeated and uncorrected misrepresentations and omissions. (*See*, for example, Petition, p. 19; S.App. 155-59) Respondents' statements throughout their Brief in Opposition that there was no evidence regarding such reliance and causation after the merger was called off are thus patently false. Moreover, respondents do not address the fatal defect in the "superseding cause" reasoning of the Court of Appeals, namely that the entire process which led to Sundstrand's damage, including the rendering of any legal opinion, was set in motion solely by respondents unlawfully inducing Sundstrand to enter into the January 9, 1969 agreement in the first instance, a wrong that respondents do not now contest.

Respondents seek to defend the improper conduct of the Court of Appeals in going outside the trial record, in order to make the crucial *appellate* finding leading to the massive

* A mistake of law can occur only when all relevant facts are known. E.g., *Dampskibs Aktieselskabet Thor* v. *Tropical Fruit Co.*, 281 F. 740, 743 (2d Cir. 1922); *State ex rel. McCormack* v. *American Building & Loan Ass'n*, 150 S.W.2d 1048, 1065 (Tenn. 1941).

reduction of the nearly $7,000,000 judgment, by characterizing that conduct as merely an effort to seek corroboration of material that was in the trial record. The Court of Appeals, however, offered no such rationale for its frolic through the record of pretrial discovery, and in its May 18, 1977 Order conceded that it had relied heavily on testimony not in evidence and thought it appropriate to do so. (S.App. 110-11) The undeniable fact is that the Court of Appeals relied upon material outside the trial record in order to make findings which were directly contrary to amply supported findings made by the District Court. Respondents offer no authority purporting to justify this conduct of the Court of Appeals, nor do they address the authorities to the contrary cited by petitioner. (Petition, pp. 22-23) This Court should not permit the adjudicatory process to be so corrupted and should reaffirm the long established limits of appellate review which have been brazenly ignored in this case by the Court of Appeals.

CONCLUSION

For the reasons given herein and in the petition for certiorari, we pray that the writ be granted.

Respectfully submitted,

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